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Supervisor Don Knabe
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FROM: J. Tyler McCauley 
Auditor-Controller

SUBJECT: **COMMUNITY DEVELOPMENT COMMISSION – FISCAL REVIEW**

At the request of the Fifth Supervisorial District, we have completed a review of the Community Development Commission's (Commission or CDC) fiscal operations. Our review focused on the implementation status of recommendations from our May 2000 fiscal review of the Commission in key areas such as procurement, payroll/personnel, contracting and travel. We also reviewed CDC's budgetary performance, and evaluated whether CDC has instituted comparable budgetary and accounting controls as those required by County departments. Finally, we reviewed CDC's City of Industry and County Business Loan Programs to ensure adequate mechanisms are in place for distributing and monitoring program funds.

Results of Review

The May 2000 fiscal review included 95 recommendations and we reviewed the implementation status of 38 (40%) recommendations. The Department has fully implemented 18 recommendations, has partially implemented 10 recommendations, and has not implemented 10 recommendations. We also made additional recommendations to further enhance the Commission's budgetary and accounting practices, procurement and contracting operations, payroll processes, and the monitoring of its Industry loans.

We found the Commission has consistently operated within its budget for the two-year period ended June 30, 2003, and that it was performing its basic accounting procedures in a satisfactory manner. The Commission should seek clarification from the Board regarding the Commission's budget amendment authorization limits; continue to

improve its procurement and contracting operations; and improve its monitoring of developer residual receipts for the City of Industry Loan Program. The following is a summary of our findings.

Budget Amendment Authorizations

Commission policies grant CDC's Executive Director the authority to transfer unlimited amounts within the same budget unit without having to obtain Board approval. In our previous review, we recommended CDC request that the Board formally grant the Commission this authority. CDC requested and obtained the Board's approval in June 2000. CDC's request to the Board did not include a dollar limitation.

Currently, County departments must comply with established controls of obtaining CAO or Board approval, depending on the dollar amount of the transfer, to transfer funds within the same budget unit. For example, after the Board approves the budget, County departments must obtain approval from the Board of Supervisors for budget adjustments in excess of \$250,000 per quarter. CDC's Executive Director has the authority to make budget adjustments throughout the year within the same budget unit without having to obtain Board approval. Although the Commission was adhering to its own policies and procedures, we are recommending the Commission clarify the Board's intent to grant CDC **unlimited** budget adjustment authority.

Procurement

We identified deficiencies in the Commission's purchasing functions similar to those noted in our original review. Specifically, we noted the Commission needs to improve its procedures for documenting price quote information; ensure Blanket Purchase Orders are used in a consistent manner; and clarify its policies for acknowledging and documenting the receipt of goods and services prior to paying invoices.

Contracting

We noted the Commission can improve its solicitation documents by ensuring prospective bidders are clear on the evaluation process. Specifically, the evaluation documents should fully disclose the purpose of the oral interview; should require bidders to provide all the necessary documentation (e.g., certifications, licenses, etc.); and should include relevant and significant minimum requirements in the RFP. In addition, the Commission can improve its evaluation process by ensuring panel members sign conflict of interest affidavits prior to evaluating proposals, and ensuring an appropriate mix of program and non-program staff comprise evaluation teams.

Loan Programs

For the City of Industry Loan Program, the Commission receives loan repayments from developers based on a percentage of the housing development's residual receipts, which essentially equals revenue less expenses on a cash flow basis. The Commission

uses repaid Industry loan amounts to fund additional Industry loans. To ensure the timely collection of loan repayments, CDC needs to ensure developers submit separate residual receipt calculations; review all Industry loans to determine if developers correctly reported and paid residual receipts to date; and require developers to pay CDC the required portion of residual receipts. In addition, the Commission can improve some administrative and documentation issues related to the Industry and County Business Loan Programs.

Review of Report

We discussed the results of our review with Commission management. The Commission's detailed response (attached) indicates agreement with many of our findings and recommendations. However, there are a number of areas in which the Commission disagrees with our report. In some instances, the Commission's response does not address the specific findings or recommendations. The following are examples where CDC takes exception to our findings/recommendations:

Budget Amendment Authorizations - Recommendation #1 - We recommended the Commission obtain clarification from the Board of Supervisors whether or not the Board intended to grant CDC's Executive Director ***unlimited*** authority to transfer funds within the same budget unit ***regardless of the dollar amount***. The Commission objects to our recommendation for a number of reasons. They believe that the Board has already delegated the authority to transfer funds within the same budget unit to the Commission based on their Board request and approval of June 2000; they indicate that they maintain full control over budgetary expenditures; they believe the Auditor-Controller had a chance and should have raised the concern of the ***unlimited*** authority back in 2000 when CDC requested the Board to delegate to CDC the authority to transfer existing appropriations between expenditure types.

Encumbrance Accounting – Recommendation #6 - CDC's response does not address the fact that the contract module of its accounting system does not reserve funds or reduce available appropriations, and therefore does not prevent CDC from over-committing its budget. Encumbering the full amount of contracts upon execution would accomplish that objective.

Timeliness of Payments – Recommendation #12 - CDC's response indicates that in determining timeliness of payments, we only allowed the Commission one week to pay its vendors when in fact we allowed 30 days for payment, which is consistent with CDC's policy.

Adherence to CDC Budget – Recommendation #9 - CDC's response implies that we are questioning CDC's budgetary performance, or the requirement for CDC to recognize revenue for the City of Industry funds in the year received. Our issue is that in current years, CDC budgets revenue that CDC already received and recognized in a prior year. This distorts CDC's revenue budget. In order to balance the budget, CDC should

classify revenue received and recognized in a prior year as a source of financing other than revenue (i.e., "other available financing").

Office of Small Business - Recommendations 32 through 34 - We agree with CDC's response that with the transfer of this program to the Internal Services Department (ISD) effective January 2005, these recommendations are no longer applicable for the Commission. As appropriate, we will work with ISD to ensure the recommendations are implemented.

For the remaining recommendations, we will continue to work with the Commission, as necessary, to correct and/or to clarify these and other issues cited in the Commission's response. We thank CDC management and staff for their cooperation and assistance during our review.

If you have any questions regarding this report, please contact me or have your staff contact Terri Kasman at (626) 293-1121.

JTM:MMO:TK
Attachments

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Los Angeles County

Community Development Commission

Fiscal Review

March 2005

Prepared by:

Department of Auditor-Controller

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Community Development Commission

Fiscal Review

Comments and Recommendations

Background

The Board of Supervisors (Board) created the Community Development Commission as an at-will, non-civil service agency in 1982. The Commission is a consolidation of the Housing Authority, the Redevelopment Agency and portions of the Community Development Department with a common Executive Director. The Housing Authority, while part of the Commission, remains a separate legal entity. Members of the Los Angeles County Board of Supervisors serve as the governing Board of Commissioners of the Commission and the Board of Commissioners of the Housing Authority. Throughout our report, the term Commission or CDC is used to describe the consolidated agency, unless otherwise noted.

CDC's mission is to effectively generate and use resources to provide housing and community development services to improve the quality of life and environment for individuals, families and communities. The Commission is funded primarily by the U.S. Department of Housing and Urban Development (HUD). Major programs funded by HUD are Section 8 Housing Assistance, Public Housing Conventional, HOME and Community Development Block Grant. The Commission's Fiscal Year (FY) 2004-05 approved budget is \$363 million. As of July 2004, the Commission employed 537 regular employees, 170 contract employees and 11 temporary employees.

At the Board's direction, the Commission has established its own accounting, budgeting and personnel systems, and related policies and procedures. The Commission developed these policies with Board approval in order to comply with the operating, administrative and fiscal requirements of its funding sources.

Scope and Objectives

The purpose of our review was to determine the implementation status of recommendations from our May 2000 fiscal review in the following areas: budget, procurement, payroll/personnel, contracting and travel. We also reviewed CDC's budgetary performance, and evaluated CDC's budgetary and accounting controls. Finally, we reviewed CDC's City of Industry and County Business Loan Programs to ensure adequate mechanisms are in place for distributing and monitoring program funds.

Budgetary Controls

As part of our review, we compared the Commission's budgetary and accounting practices to those required by the County to determine if the Commission can strengthen its budgetary and accounting practices. Specifically, we reviewed the

Commission's procedures over the reporting and/or controlling of budget amendment authorizations, budget administration, capital projects, encumbrances, unanticipated revenues and budget status reports.

Budget Amendment Authorizations

County departments and agencies must obtain Board approval to amend the original budget. The Chief Administrative Officer has been delegated the authority to amend the original budget and is allowed to approve transfers of appropriations between expenditure types within the same budget unit up to \$250,000 per quarter; transfers in excess of \$250,000 must be approved by the Board of Supervisors. This control was established by the Board to limit department's discretion to adjust budgets that the Board already approved.

In our May 2000 review, we noted that the Commission's November 1984 internal policy allowed the Executive Director to transfer funds of any amount within the same budget unit. Since we were unable to confirm whether the Board of Supervisors actually granted this authority to the Commission's Executive Director, we recommended that CDC request the Board formally grant him the authority.

To comply with our audit recommendation, CDC issued a letter to the Board of Supervisors in June 2000, requesting the Board delegate to CDC's Executive Director the authority to transfer existing appropriations between expenditure types within the Commission's approved budget. In our opinion, CDC's request to the Board was not clear to the extent that a dollar limitation (similar to the existing dollar limitation of \$250,000 where departments must obtain Board approval) was not included on CDC's request to the Board. Currently, all other County departments must comply with established controls of obtaining CAO or Board approval, depending on the dollar amount of the transfer, to transfer funds within the same budget unit.

It should also be noted that CDC management strongly believes that they in fact have delegated authority to make such transfer of funds. While we are not disagreeing that the Board granted CDC the authority to transfer the funds without Board approval, we continue to believe that CDC should obtain clarification from the Board of Supervisors in their intent to grant CDC ***unlimited*** authority to transfer funds within the same budget unit ***regardless of the dollar amount***.

We consider the recommendation related to obtaining Board approval to transfer appropriations between expenditure types to be implemented.

Recommendation

- 1. Commission management clarify with the Board whether or not the Board intended to grant CDC's Executive Director *unlimited* budget adjustment authority.**

Budget Administration

County departments notify the CAO and the Auditor-Controller's Accounting Division of all budget adjustments, regardless of the amount, to ensure the availability of funds and to ensure the accurate reporting of departmental final adjusted budgets in the County's final budget. The Commission is not part of this process.

We noted that the official "2003-2004 Final County Budget" did not contain the Commission's final adjusted budget for FY 2002-03. We also noted that the Commission's internally generated budget book for FY 2003-04 did not reflect the adjusted budget for FY 2002-03.

To provide accurate and timely budget data, CDC management, in conjunction with the CAO, should establish procedures to annually report its final adjusted budget to the CAO for inclusion in the official Final County Budget. In addition, to ensure budget data reported is meaningful and to avoid the appearance of overspending, CDC management needs to ensure mechanisms are in place for reporting adjusted budgets in its internally generated budget book.

Recommendations**Commission management:**

- 2. In conjunction with the CAO, establish procedures to annually report its final adjusted budget to the CAO for inclusion in the official Final County Budget.**
- 3. Ensure mechanisms are in place for reporting adjusted budgets in its internally generated budget book.**

Capital Projects

In FY 2003-04, CDC reported a capital project budget of \$7.3 million, consisting of eight distinct projects.

In our original review, we noted that CDC's practice was to develop an internal budget for each capital project, but not to consider each capital project as a distinct budget unit for Board approval. This practice was not in compliance with Los Angeles County policy (County policy) which requires County departments to establish a separate budget unit for each capital project. The purpose of the County policy is to ensure that capital projects are budgeted for at the project level so that the responsibility for transfer of budgetary appropriations between budget units is centralized with the Board or a Board-delegated agency. Accordingly, we recommended Commission management adopt the capital budgeting practices and procedures required by County policy.

To comply with our audit recommendation, Commission staff with the assistance of Auditor-Controller staff developed an Administrative Policy for establishing a capital projects budget. Specifically, the Policy defines what constitutes a capital project and how CDC will report their capital projects budget to the Board at the beginning of each fiscal year. However, the policy does not require each capital project to be accounted for in a separate budget unit as recommended in our original review. Accordingly, the Commission can continue to improve its capital projects' reporting practices by establishing each capital project as a separate budget unit and seeking Board approval throughout the year to shift funds between or among individual capital projects.

We consider the recommendation relating to the adoption of capital budgeting practices and procedures to be partially implemented.

We also noted the Commission has not established each capital project as a distinct budget unit on its accounting records. Commission staff stated that its PeopleSoft budgetary and accounting system lacks the ability to establish numerous budget units. Accordingly, the Commission tracks the activities of each capital project on Microsoft Excel spreadsheets. Commission staff stated that the cost of restructuring its PeopleSoft budgetary and accounting system to accommodate numerous budget units would outweigh the benefit. However, Commission staff could not demonstrate that it had performed a cost analysis to support their statement. CDC needs to evaluate and document the feasibility of establishing separate budget units for its capital projects through its existing accounting system.

Recommendations

Commission management:

- 4. Seek Board approval to shift funds between or among separate capital projects and/or budget units.**
- 5. Evaluate and document the feasibility of establishing separate budget units for its capital projects through its existing PeopleSoft accounting system.**

Encumbrance Accounting

Encumbrances are obligations that are represented by purchase orders, contracts, or other binding legal requirements and reduce the amount of available spending authority because they will result in actual expenditures. Encumbrances are used as a budgetary control to ensure that the current year's resources are not over expended.

For the County, encumbrances are established in the Countywide Accounting and Purchasing System (CAPS) for the full amount of a contract or obligation upon execution. CAPS records, tracks and controls departmental encumbrances and expenditures and prevents departments from exceeding appropriations.

CDC uses the PeopleSoft budgetary and accounting system to record, track and control its financial transactions. Like CAPS, PeopleSoft has built in controls to prevent the overspending of individual contracts. However, the Commission does not consistently encumber, or reserve, the full amount of its single-year contracts upon execution. Instead, Commission staff usually encumbers funds for a portion of the contract amount. Failure to encumber the full contract amount upon execution could result in the following:

- The Commission could over-commit its total spending authority (appropriation) if funds for legal obligations such as contracts are not encumbered or reserved.
- The Commission's accounting records will not reflect its full legal obligations.
- The Commission will not be able to meet its legal (contractual) obligations should funding become exhausted.

To ensure the Commission does not exceed its spending authority and to ensure adequate disclosure of contractual obligations, Commission management should encumber the full amount of contracts upon execution.

Recommendation

- 6. Commission management encumber the full amount of single-year contracts (or other binding legal obligations) upon execution.**

Administrative Policies and Procedures Update

The Commission's Administrative Policies and Procedures (Administrative Policies) have not been updated since November 1984 and do not address all of the Commission's budgetary processes. For example:

- Government Code Section 29130 requires County departments to obtain Board approval when they receive additional revenues that were not included in the budget or in excess of the budgeted amount. While the Commission's practice is consistent with the requirements of the Code and County policy, it needs to be included in the Commission's Policy.
- The current Administrative Policies do not address the Commission's practice of preparing periodic budget status reports.
- The current Administrative Policies do not address the process for reporting budget data to the CAO for inclusion in the official Final County Budget.

To ensure staff has current policies and procedures, CDC needs to update its Policy to reflect its unanticipated revenue procedures and other current budgetary and accounting practices.

Recommendation

- 7. Commission management update its Administrative Policies and Procedures to reflect its unanticipated revenue procedures and other current budgetary and accounting practices.**

Budget Status Reports

County departments prepare and submit periodic Budget Status Reports (BSRs) to the CAO for review. BSRs provide a comparison between the department's estimated actual revenue and expenditures and their approved annual budget. The CAO reviews these reports to ensure that County departments do not exceed or under spend their budget and allows departments to shift funds, if necessary, to meet financial obligations in a timely manner. The Commission's practice is to prepare periodic budgetary status reports for review by the Commission's Executive Office of Budget, (instead of the CAO) on an as-needed basis.

We noted that for FY 2002-03, the Commission completed only two budget status reports and in FY 2003-04 the Commission only completed one budget status report. The BSR, when prepared regularly, is a good monitoring tool because it provides management with the information needed to make timely decisions regarding its budget. Commission management should develop and implement a policy requiring division staff to complete budget status reports on a consistent basis (i.e., quarterly) and to submit these reports to the Executive Office of Budget for review.

Recommendation

- 8. Commission management develop and implement a policy requiring division staff to complete budget status reports on a consistent basis (i.e., quarterly) and to submit the reports to the Executive Office of Budget for review.**

Adherence to CDC Budget

In examining the Commission's adherence to its budget, we compared the Commission's actual financial results to its adjusted budget for FYs 2001-02 and 2002-03. The results are summarized below:

**Budget to Actual Financial Results
Fiscal Year 2001-02**

	Budget	Actual	Over or (Under)
Expenditures	\$ 361,919,952	\$ 319,524,738	\$ (42,395,214)
Revenue	\$ 361,722,687	\$ 307,414,905	\$ (54,307,782)
Difference	\$ (197,265)	\$ (12,109,833)	\$ (11,912,568)

**Budget to Actual Financial Results
Fiscal Year 2002-03**

	Budget	Actual	Over or (Under)
Expenditures	\$ 362,392,296	\$ 346,814,828	\$ (15,577,468)
Revenue	\$ 362,394,064	\$ 334,229,100	\$ (28,164,964)
Difference	\$ 1,768	\$ (12,585,728)	\$ (12,587,496)

Overall, the Commission has operated within its budget. However, the Commission has under-realized revenues of approximately \$54 million and \$28 million during the last two fiscal years, and actual expenditures were under budget by approximately \$42 million and \$16 million, respectively. We analyzed these variances and noted the budget variances are primarily attributable to:

- Delays encountered by CDC in completing construction projects, due to unforeseen construction delays (e.g., unforeseen site conditions; developer financing problems, etc.). As a result, construction expenditures were not incurred and the associated program revenues were not realized.
- The Commission's presentation of its revenue budget. For example, the shortfalls of \$12.1 million and \$12.6 million for FYs 2001-02 and 2002-03, respectively, are primarily the result of the Commission over-budgeting revenue by almost \$10 million in both fiscal years for City of Industry funds received and recognized as revenue in 1998. Instead, from a presentation stand point, the Commission should have budgeted the \$10 million as "available financing" (i.e., fund balance) in FYs 2001-02 and 2002-03, so as to not distort their budgeted revenue for these two FYs.

Budgets help to facilitate control over revenues and expenditures. Budgets also provide the most benefit when they represent the best estimate of actual expected results. Accordingly, the Commission needs to re-evaluate the method used to present its revenue budget for City of Industry funds in its accounting records and for financial reports to better reflect their budgeted financial position.

Recommendation

- 9. Commission management re-evaluate the method used to present its revenue budget for City of Industry funds in its accounting records and financial reports to better reflect their budgeted financial position.**

Procurement

In our original review, we noted that the Commission's Procurement Unit was not providing the necessary level of control and monitoring to ensure the Commission's purchasing function was operating in accordance with established guidelines and procedures.

In our current review, we evaluated the implementation status of 11 recommendations previously made related to procurement. CDC has implemented two of the 11 recommendations, has partially implemented three recommendations, and has not implemented the remaining six recommendations. We also developed an additional six recommendations related to the overall improvement of the Commission's procurement operations.

Purchase Order Changes

The Commission's Purchasing Policies and Procedures Manual (Purchasing Manual) includes procedures to change established purchase orders. Specifically, the requestor must justify changes and limit changes to the dollar amount of the purchase order to no more than 25% of the original total dollar amount. Staff are required to consider change orders that do not satisfy these requirements as new procurements.

In our original review, we noted instances in which staff should have denied purchase order changes because requestors did not justify the changes, and requests to increase the dollar value of purchase orders were greater than 25% of the original total amount. We also noted that the Commission should update its Purchasing Manual to include procedures for authorizing purchase order changes.

In our current review, we noted the Commission's Purchasing Manual did not include the specific authorizations necessary for change orders. We selected 15 purchases where CDC augmented the original dollar amount of the purchase order to determine if CDC complied with established change order procedures. We noted that 13 (87%) of the 15 change orders were processed in accordance with CDC policy. For the remaining two change orders, we noted the following:

- For one (7%) purchase, staff did not adequately document the reason(s) for the change.

- For one (7%) purchase, the dollar increase was within the authorizers' limit. However, the final total dollar amount of the purchase order was not within the limit of the person that approved it.

We consider the recommendation related to CDC revising its Purchasing Policies and Procedures Manual to be not implemented, and the recommendation related to complying with established change order procedures to be partially implemented.

Solicitation of Quotations

In our original review, we recommended the Commission evaluate requiring written bids for purchases that exceed \$5,000, but which are less than \$25,000. We also recommended the Commission require staff to consider all cost information (e.g., shipping costs, discount terms, tax, etc.) when calculating bids and to obtain all information (e.g., vendor name, telephone number, contact person(s), price quotes for all items to be purchased, date of the quotation, etc.) required by its Purchasing Manual when obtaining price quotations.

During our follow up we noted that CDC changed its policy requiring staff to document three price quotations for purchases between \$1,000 and \$24,999. This policy is not reflected in the Purchasing Manual.

We selected a sample of ten purchases between \$1,000 and \$24,999 and noted the following:

- For one (10%) purchase, Commission staff did not document three price quotes as required by policy.
- For nine (90%) purchases, we were unable to determine whether staff considered all cost information (e.g., shipping costs, discount terms, tax, etc.) when calculating bids, because the form on which staff document quotes does not separately itemize these costs.
- For eight (80%) purchases, Commission staff did not document all price quote information (e.g., date of quotation, vendor contact person, telephone number, etc.) required by Commission policy.

We consider the recommendation requiring the Commission to evaluate the appropriateness of having staff obtain written bids to be implemented, and the recommendations relating to obtaining all cost information and all other information (i.e., vendor name, telephone number, etc.) to be partially implemented.

Commission management needs to ensure staff document at least three price quotes for purchases between \$1,000 and \$24,999 and document these procedures in its Purchasing Manual.

Recommendation

- 10. Commission management ensure staff document at least three price quotations for purchases between \$1,000 and \$24,999 and document the procedures in its Purchasing Manual.**

Matching Payment Documents

A generally accepted internal control practice is to compare vendor invoices with purchase order terms and reports of goods received before paying the invoices. This ensures payments are made for goods or services actually ordered and received and that the correct price is paid. The person receiving goods and certifying quantities received should not be associated with nor have responsibilities related to ordering the goods or accounting for purchases.

In our original review, we noted that 83% of the invoices sampled were paid without evidence the goods were actually received, and 17% of the invoices sampled had a packing slip which was inappropriately signed by the requester of the item purchased.

During our follow up review, we selected a sample of 15 purchase orders processed during calendar year 2003, totaling approximately \$238,000. We noted that Accounts Payable continues to process payments without a packing slip or other evidence that the goods were actually received. We also noted that division staff used inconsistent methods for documenting and for acknowledging that goods/services were received. For example, some staff notate "OK to pay" while others include their initials and the date. Staff with whom we spoke could not always explain the meaning of the specific notations.

A clear, uniform method of acknowledging that services were received will expedite and assist Accounts Payable in processing payments and promote consistency among the divisions. Accordingly, CDC management needs to clarify its policies for acknowledging and documenting the receipt of goods and services.

We consider the recommendations related to matching payment documents, ensuring that staff who receive goods/services did not order the goods/services, and Accounts Payable staff returning all requests for payment that do not include documentation of receipt of goods to be not implemented.

Recommendation

- 11. CDC management clarify its policies for acknowledging and documenting the receipt of goods and services.**

Stamping Invoices “Paid”

In our original review, we noted that 19 (95%) of 20 invoices we reviewed were not stamped “paid” after Accounts Payable issued payment. Accordingly, we recommended Commission management require Accounts Payable staff to stamp invoices “paid” to prevent reuse or duplicate payments. In our follow up, we selected 30 invoices for review and noted that all 30 were stamped “paid” to prevent reuse. Accordingly, this recommendation has been implemented.

We consider the recommendation related to stamping invoices “paid” to be implemented.

Timeliness of Payments

In our original review, we noted that nine (45%) of 20 payments we reviewed were not made within the required time frame. CDC stated that its policy is to pay approved and documented invoices within the vendor’s specified timeframes, which is generally within 30 days of receipt of the vendor’s invoice. Accordingly, we recommended staff submit payment requests that are properly documented in sufficient time to ensure the vendor is paid timely.

In our current review, we noted that Accounts Payable staff did not process 8 (27%) of 30 payments within the required time frame, including one that was approximately 50 days late. It should be noted that there were no lost discounts as a result of the late payments. We also noted that Division staff did not stamp the invoice with the date received. Accordingly, we calculated the number of days past due by comparing the invoice date plus one week to the date paid.

We consider the recommendation relating to the timely payment of vendor invoices to be not implemented.

Recommendations**Commission management:**

- 12. Ensure staff pay invoices within the required time frames.**
- 13. Require Division staff to date stamp invoices upon receipt.**

Blanket Purchase Orders

BPOs provide for the purchase of goods/services up to a maximum dollar amount with a specific vendor for a fiscal year. This type of purchasing method allows for multiple smaller dollar purchases without having to bid each purchase. It also allows management to identify frequently purchased items, assess the need to enter into agreements with vendors to obtain favorable purchasing terms, and limits and controls

the number of purchase orders used throughout the year for frequently purchased items.

In our original review, we noted instances in which staff requested multiple increases to a purchase order throughout the year and did not consider the use of agreement Blanket Purchase Orders. Accordingly, we recommended Commission management utilize BPOs when possible.

In our current review, we selected 20 purchases to determine if any should have been processed as agreement BPOs. For eight (40%) of the 20 purchases, CDC appropriately used an agreement or contract to procure the goods or services. For the remaining 12 (60%) purchases, CDC did not use BPOs as previously recommended.

- **For four (20%) purchases, CDC established four separate BPOs for the same service and vendor.** Commission staff established four separate BPOs, each for the procurement of uniform/rug rentals, totaling \$9,700. The Commission should have established one BPO at the beginning of the year for the estimated amount of uniform/rug rentals.
- **For three (15%) purchases, the Commission established new procurements when a contract or BPO already existed for the same service and vendor.** For example, Commission staff established two purchase orders, totaling \$1,150, for asbestos testing services. However, the Commission had an existing contract with this vendor for the same service, and sufficient available funding on the contract to process the above two purchases.
- **For five (25%) purchases, the Commission established new procurements when they should have established a BPO.** Staff established the five purchase orders with two different vendors for the procurement of plumbing and heating services between October 2003 and January 2004. However, the Commission could have established one BPO with one vendor for the procurement of these services. Although each individual purchase was within the authorizers' limit, the combined total of these purchase orders would have required approval at a higher level had the Commission established one BPO at the beginning of the year.

Commission management stated that they do not utilize BPOs on a Commission-wide basis because the Divisions wish to control their portion of the purchases. However, utilizing BPOs in the manner intended should not limit or restrict Divisions' ability to control purchases. Staff can amend BPOs during the year to reflect changes (increases or decreases) in their needs, and Purchasing can establish "sub-order" systems, assigning a block of numbers to each Division so that Divisions can control their "portion" of the funding under a Commission-wide BPO. Commission staff also stated that they do not want to restrict the funds by establishing one Commission-wide BPO at the beginning of the year for the estimated annual expenditures, in the event they can re-bid some of the purchases to obtain more favorable pricing. However, the purpose of utilizing BPOs is to obtain the most favorable pricing.

To ensure the efficiency and effectiveness of the Commission's purchasing operations, CDC management should work with the County's Internal Services Department (ISD) regarding the proper utilization of BPOs. In addition, in conjunction with ISD, Commission management should evaluate its system capabilities for establishing a "sub-order" system for monitoring and controlling BPO-related expenditures. This recommendation should be implemented in conjunction with the centralization of the Commission's purchasing operations.

We consider our previous recommendation relating to the utilization of BPOs to be not implemented.

Recommendations

Commission management:

- 14. Work with the Los Angeles County ISD regarding the proper utilization of BPOs.**
- 15. In conjunction with ISD, if appropriate, evaluate its system capabilities for establishing a "sub-order" system for monitoring and controlling BPO-related expenditures.**

Contracting

In our original review, we noted the Commission could benefit from the development of centralized oversight for its procurement function and increased training of staff on contracting policy and process. We made 13 recommendations related to the improvement of the Commission's contracting operations, including the establishment of a Contract Manager position responsible for policy formulation, training and review processes. In our current review, we evaluated the implementation status of 11 recommendations related to contracting and noted that CDC has implemented five of the 11 recommendations, has partially implemented four recommendations, and has not implemented the remaining two recommendations. During FY 2003-04, CDC issued 249 contracts valued at approximately \$20 million.

Our current review disclosed that the Commission has established a contract manager position, as previously recommended. However, the Commission needs to continue to improve its documentation for soliciting, evaluating and scoring proposals.

Oversight Responsibilities

In our original review, we recommended Commission management establish a position of Contract Manager in the Central Services Unit, responsible for policy formulation, training and review processes. In our current review, we noted the Commission established a Contract Manager position in the Central Services Unit effective April 2001. The Contract Manager is responsible for reviewing contracts, conducting training

for purchasing related functions, assisting Division staff with implementing Section 3 purchasing requirements and facilitating the purchasing help desk.

We consider the recommendation to establish a position of Contract Manager to be implemented.

Solicitation Process

We reviewed the solicitation process related to Community Policing and Investigative Services (Policing) and Consultant Services (Consulting) contracts initiated by the Housing Management Division and the Housing Development and Preservation Division, respectively. Specifically, we reviewed: (1) the solicitation document to determine if it provided an adequate explanation of the proposal evaluation process, including the evaluation criteria; (2) the proposal evaluation instruments to determine if they provided an objective basis for evaluating panel member scoring; and (3) the composition of the evaluation team and the processes it used in scoring the proposals to determine if they were fair, reasonable and consistent.

Solicitation Documents

We reviewed the Request for Proposal (RFP) documents used to solicit potential proposers to provide Policing and Consulting Services. Specifically, we found that:

- For both solicitations, the RFP did not explicitly describe the purpose of the oral interview (e.g., for clarification purposes, decision making, or evaluation of proposers ability).
- The RFP for the Policing solicitation did not require proposers to provide all the necessary documentation (e.g., certifications, licenses, etc.) to ensure that qualified staff are assigned to the project.
- The RFPs for both solicitations did not disclose minimum requirements (pass/fail) that proposals must meet before the proposals would be evaluated. For example, a minimum number of years experience in providing community policing in housing developments for the Policing solicitation.

For future solicitations, the Commission should ensure that the evaluation documents fully disclose the purpose of the oral interview and require proposers to provide all the necessary documentation (e.g., certifications, licenses, etc.) to ensure that qualified staff are assigned to the project. In addition, the Commission should include relevant and significant minimum (pass/fail) requirements in the RFP.

Recommendations

Commission management:

- 16. Ensure that the evaluation documents fully disclose the purpose of the oral interview.**
- 17. Require proposers to provide all the necessary documentation (e.g., certifications, licenses, etc.).**
- 18. Include relevant and significant minimum requirements in the RFP.**

Proposal Evaluation Instrument

We reviewed the evaluation instruments used to evaluate the written proposals for two solicitations (Policing and Consulting Services). We noted that the instruments assigned evaluation criteria and weights. However, we noted several areas where enhancements can be made to ensure continued integrity of the evaluation process. Specifically:

- **For both solicitations, the questions on the evaluation instrument could be restated or expanded to provide evaluators with a better basis to support the evaluator's rating.** For example, for the Policing solicitation, the questions regarding the bidder's previous experience could be expanded so that points are given to specifically reflect the number of years of experience (e.g., 1 point for one to two years of experience, 3 points for three to four years of experience, and 5 points for more than five years of experience, etc.).

We consider our recommendation related to providing evaluators with specific, detailed, and objective rating categories and sub-criteria and explanations/instructions to rate these areas as partially implemented.

- **The questions on the evaluation instrument did not address the functions being evaluated.** For example, the RFP used for Policing Services identifies two distinct services (e.g., community policing and narcotic investigations) the Commission wants potential contractors to provide. However, CDC used one evaluation instrument for both services and the questions on the instrument did not include a series of questions to measure or distinguish the specific services to be performed.
- **The instrument used for Consulting Services did not have adequate space for evaluators to comment on their scores.** In our original review, we noted that none of the evaluation forms we reviewed contained space for evaluators to document how they arrived at their scores.

In our current review, we noted that evaluators did not include written comments to support their scores in one or more sections in 14 of the 15 instruments we reviewed. This may be in part due to inadequate space provided on the evaluation instrument.

We consider our recommendation related to providing evaluators with sufficient space to document how they arrived at their scores as not implemented.

To ensure that the evaluation process measures and distinguishes the specific services to be performed, Commission management should ensure that the questions on the evaluation instrument address distinct functions being evaluated.

Recommendation

- 19. Commission management ensure that the questions on the evaluation instrument address the distinct functions being evaluated.**

Evaluation Process

Evaluation Committee

In our original review, we recommended the Commission require evaluators meet to compare and summarize the evaluations and document the committee's selection process. We also recommended the Commission consider limiting the number of evaluators to a manageable number. In our current review, we noted that the committees were knowledgeable to give a reasonable evaluation. However we noted a number of deficiencies in the Department's evaluation process. Specifically:

- **Committee members did not resolve differences in scoring or explain their rationale for large scoring discrepancies.** As a result, some evaluation criterion and sub-criterion had unresolved differences in the individual scores assigned by committee members. For example, for the Policing solicitation, one evaluator assigned a proposer zero points (out of a possible 15 points) for the criterion "Overall Approach", while another evaluator assigned the same proposer the full 15 points. The evaluator who assigned zero points provided written comments that indicated the proposer did not submit the information requested, while the evaluator that assigned 15 points provided comments that did not specifically address the criterion being evaluated. For the Consulting solicitation, one evaluator assigned zero points (out of a possible 2 points) for the sub-criterion "Organizational Chart" and commented he could not locate the organizational chart, while another evaluator assigned the full two points and did not provide any comments.

We consider our recommendation related to requiring evaluators to meet and compare and summarize the evaluations and documenting the committee's selection process as not implemented.

- **For both solicitations, the Commission did not require evaluators to sign conflict of interest affidavits but relied on informal self-reporting.** In order to enhance the integrity of the evaluation process, Commission management should ensure that panel members sign conflict of interest affidavits or certifications prior to evaluating proposals.
- **The majority of the evaluation panel that evaluated proposals for the Policing solicitation was comprised of Commission staff closely involved in the program.** For example, three of the four panel members worked in some capacity for the program being evaluated. Technical expertise is essential in reviewing evaluations. However, this particular panel make up could give the perception that the panel would rely on their personal knowledge and expertise rather than on the proposals themselves. In order to enhance the integrity of the process, CDC should have an appropriate mix of program and non-program staff to comprise the evaluation teams.
- **Evaluators assigned points to the reference section without checking the quality of the references.** For both solicitations, the Commission established references as an evaluation criterion, worth up to ten points, but did not require evaluators to verify the references or provide evaluators with criteria upon which to evaluate the references. For example, for the Consulting solicitation, proposers could receive five points for providing a list of four references familiar with the proposer's work, and an additional five points for including the references' contact information. In this case, a proposer could receive the full ten points even if a reference was unhappy with the proposer's work performance.

A generally accepted method for evaluating proposers' references is for departments to include references as an evaluation criterion. One designated staff person develops a list of questions to ask each reference, evaluates or scores the references' responses and determines whether the references' responses were favorable or not towards the proposer. Accordingly, Commission management should establish guidelines for determining the appropriate weight and the specific criteria for evaluating references.

Recommendations

Commission management:

20. **Ensure that panel members sign conflict of interest affidavits or certifications prior to evaluating proposals.**
21. **Ensure an appropriate mix of program and non-program staff comprise evaluation teams.**
22. **Establish guidelines for determining the appropriate weight and specific criteria for evaluating references.**

Proposal Scoring

For both solicitations, staff stated they calculated proposers' final scores using the averaging scoring methodology (an average of the evaluators' individual scores). However, the Commission did not document this scoring methodology or the method to arrive at final scores. We recalculated the final scores using the averaging scoring methodology and agreed with the Commission's final ranking. However, Commission management needs to ensure that staff document the scoring methodology and maintain documentation to support their conclusions in the contracting file.

Recommendation

- 23. Commission management ensure that staff document the scoring methodology and maintain documentation to support their conclusions in the contracting file.**

RFPs/RFQs

We reviewed five contracting records, including signed contracts and solicitation documents, among five Divisions to determine if the Commission has implemented the recommendations from our prior review related to contract administrative processes. Our review disclosed the following:

Outreach Efforts

Commission policy requires that Divisions provide vendors/contractors a minimum of 15 calendar days to prepare and submit bids/proposals, and that advertisements and notices include certain clauses in Spanish. In our original review, we noted that the Commission mailed notices of the RFP and advertised the RFP in several minority newspapers several days after the RFP's opening date. We also noted that for several other RFPs/RFQs, the Commission did not include the appropriate clauses in Spanish.

We reviewed five RFP advertisements/notices and noted that each included the appropriate clauses in Spanish. However, Divisions did not always advertise the RFP 15 days prior to the proposal due date in all required publications.

We consider the recommendation related to the Commission providing vendors with a minimum of 15 calendar days to prepare and submit bids/proposals to be partially implemented, and the recommendation related to including the applicable clauses in Spanish in contracting advertisements and notices to be implemented.

Section 3 Procurement Procedures

In our original review, we noted that there was significant confusion regarding Section 3 guidelines among staff that we interviewed. In general, Section 3 of the Housing and

Urban Development (HUD) Act of 1968 ensures that employment, training, contracting and other economic opportunities generated by HUD financial assistance is directed to low and very low income persons. We recommended CDC management re-write the Section 3 guidelines to make them easier for staff to understand. We also recommended CDC management ensure that staff responsible for procurement clearly understand and are able to identify the funding sources (and associated thresholds) that trigger Section 3 contracts as well as require that managers apply the Section 3 procurement policy, if applicable.

In our current review, we noted that CDC developed and distributed a Section 3 Compliance Plan (Plan) to managers and staff. The Plan provides more detailed and comprehensive guidelines for processing and identifying Section 3 procurements when compared to guidelines presented in the Purchasing Manual.

We also noted that the Commission established a position of Compliance Officer and provided additional training to staff responsible for processing Section 3 procurements. In addition, we reviewed five Section 3 contract files to determine whether staff appropriately identified these contracts as Section 3 procurements and whether these procurements met the Section 3 procurement requirements. We noted no exceptions.

We consider the recommendations related to re-writing the Section 3 guidelines and ensuring staff clearly understand and are able to identify the funding sources (and associated thresholds) that trigger Section 3 contracts to be implemented.

Disclosures

The Commission's Purchasing Manual requires the inclusion of specific disclosures in RFPs and subsequently awarded contracts. In our original review, we noted that contract files reviewed did not routinely include these required disclosures. We recommended Commission management require staff to include all required disclosures in RFPs.

In our current review, we selected five contract files to determine if staff included appropriate disclosures in its solicitation documents. We noted that in all five instances, the solicitation documents did not inform vendors of the availability of the bidders list. We also noted that the following additional disclosures, which were mandated by the Commission subsequent to our original review, were not consistently included in the five solicitation documents reviewed:

- Two (40%) RFPs did not include language disclosing the Commission's Policy on Doing Business with Small Business requirements.
- One (20%) RFP did not inform vendors of the minimum mandatory requirements (pass/fail requirements).

- One (20%) RFP did not disclose the County's Baby Safely Surrender Law requirements.

We consider the recommendation related to the Commission including all required disclosures in solicitation documents to be partially implemented.

Central Services staff indicated that they have created a centralized procurement folder giving Divisions easy access to procurement documents, including a checklist of solicitation disclosures. However, Division staff with whom we spoke stated that they do not always utilize the procurement folder to obtain the latest disclosures. CDC management should require Division staff to utilize the procurement folder to access standard disclosures and language for solicitation documents

Recommendation

- 24. Commission management ensure Division staff utilize the procurement folder to access standard disclosures and language for solicitation documents.**

Sealed Bids

The Commission generally uses a Sealed Bid process to procure services for construction projects whose cost exceeds \$25,000. In our original review, we noted that the Commission needed to improve its documentation of the bid opening process. Specifically, we recommended Commission management ensure that the Purchasing Officer or designee attends all bid openings and completes a sign-in sheet. We also recommended Commission management require staff to take meeting minutes and include the minutes in the files.

In our current review, we selected five Sealed Bids obtained by the Construction Management Division and noted that each had a completed sign in sheet indicating that the Purchasing Officer or designee attended the bid opening. In addition, we noted that Commission staff appropriately documented each bid opened, the time, date and location of the bid opening, and the signatures of witnesses when taking meeting minutes. However, staff stated that conversations material to the sealed bid proceedings are not documented. Accordingly, Commission management should require staff to take meeting minutes including documenting discussions and conclusions reached at the bid opening process.

We consider the recommendations relating to the Purchasing Officer attending bid openings to be implemented and the taking of meeting minutes to be partially implemented.

Recommendation

- 25. Commission management ensure staff documents in the meeting minutes discussions and conclusions reached at the bid opening process.**

Personnel and Payroll

In our original review, we made 12 recommendations related to the Commission's personnel and payroll operations. Specifically, we noted that the Commission needed to improve the administration of its bilingual bonus program. In addition, we noted the Commission needed to develop payroll distribution controls, and monitoring controls to prevent worker's compensation overpayments. In our current review, we evaluated the implementation status of the 12 recommendations and noted that CDC has implemented nine of the 12 recommendations, has partially implemented one recommendation, and has not implemented the remaining two recommendations. As noted below, we also made an additional six recommendations related to the overall improvement of the Commission's personnel/payroll operations.

Bilingual Bonus

CDC's Administrative and Personnel Policy Manual (Manual) permits the payment of a \$100 monthly stipend (bilingual bonus) to regular employees whose assignments require fluency in English and a second language. CDC currently has 141 employees who receive a bilingual bonus.

Authorization

In our original review, we noted CDC's Manual lacked written procedures for approving bilingual bonuses, although CDC's practice required employees to receive Division Director written authorization and to successfully complete a bilingual proficiency examination administered by Los Angeles Unified School District as a pre-requisite to receiving bilingual pay. Accordingly, we recommended CDC management revise its Manual to include a provision requiring written Division Director authorization and successful completion of a bilingual proficiency exam as prerequisites to approving bilingual pay, and to maintain documentation supporting the granting of a bilingual bonus in the employee's personnel file.

In our current review, we noted that CDC appropriately revised its Manual to include the bilingual pay pre-requisites. We also selected and reviewed 20 personnel files and noted that two (10%) of the files did not contain documentation from the testing agency verifying the employees' successful completion of the bilingual proficiency examination. In addition, CDC management stated they were unable to obtain documentation from the testing agency for 14 (47%) of 30 employees in our original review who did not have documentation of successful completion of the bilingual proficiency examination.

We consider the recommendation related to revising the Manual to be implemented and the recommendation related to maintaining documentation to be partially implemented.

Commission management should identify and re-test all employees receiving bilingual compensation that do not have proof of successful completion of the bilingual proficiency examination from the testing agency in their personnel file.

Recommendation

- 26. Commission management identify and re-test all employees receiving bilingual compensation that do not have proof of successful completion of the bilingual proficiency examination from the testing agency in their personnel file.**

Employee Eligibility

In our original review, we noted that CDC awarded bilingual bonuses to 11 contract employees whose employment contracts did not contain a bilingual bonus provision. These contract employees received bilingual pay over a period of approximately three years, at an estimated cost of approximately \$18,500. We recommended CDC either amend its current employment contract to include a provision for bilingual bonuses, or discontinue bilingual bonuses to employees whose contracts did not contain a bilingual bonus provision. We also recommended CDC management consider seeking reimbursement of bilingual bonuses paid to contract employees during periods in which their contracts did not contain a bilingual bonus provision.

CDC management indicated that they included the bilingual bonus provision in the employees' contracts as necessary. We reviewed CDC's current employment contracts for ten contract employees receiving a bilingual bonus to determine if the employment contracts contained a bilingual bonus provision. We noted that eight (80%) employees' contracts did not have a bilingual bonus provision in their current employment contract. We selected and reviewed the employees' prior year's contracts and noted the Commission did, in some instances, include the bilingual bonus provision. Commission management stated that the omission of the bilingual bonus provision in the current year's contracts was due to an oversight. Management amended all contracts requiring a bilingual bonus provision and revised the current contract template to include the bilingual bonus provision.

CDC did not seek reimbursement of bilingual bonuses paid to contract employees during periods in which their contracts did not contain a bilingual bonus provision. CDC management stated that it made a business decision to not seek reimbursement of the bilingual bonuses paid, as the contract employees had in fact provided the bilingual services.

We consider the recommendation related to amending its employment contracts to include a bilingual bonus provision to be implemented, and the recommendation related to seeking reimbursement to be implemented.

Job-Related Bilingual Fluency

In our original review, we noted that three (30%) of the ten employees interviewed did not have a job-related need for bilingual fluency. In addition, we noted that CDC's Manual did not establish the specific duties and criteria that a job assignment must meet to qualify for bilingual fluency, nor did the Manual require annual reviews of employees receiving bilingual bonuses to verify continued eligibility. Accordingly, we recommended CDC management revise its Manual to establish guidelines and restrictions on the type of job assignments eligible for bilingual pay, and review and re-certify employees' job-related need for bilingual fluency at least once annually.

In our current review, we noted that CDC revised its Manual to allow Division Directors the authority to determine whether an employee, based on job duties, is eligible to receive the bilingual bonus. CDC management stated that due to the diverse work activities performed by Commission staff and the diverse population that they serve, granting Division Director the authority to decide which job duties qualify to receive bilingual bonus provides CDC the needed flexibility to meet their business needs.

We also selected 20 employees who received bilingual compensation and reviewed their personnel files to determine if management reviewed and re-certified the employees' job-related need for bilingual fluency at least once annually, or upon employee transfer or reclassification. We noted no exceptions.

We consider the recommendations related to establishing guidelines and restrictions on the type of job assignments eligible for bilingual pay, and re-certifying employees' job-related need for bilingual fluency to be implemented.

Employee Terminations

In our original review, we noted that seven (28%) of the 25 terminations reviewed were processed after the Commission's standard time frame of 15 calendar days. We recommended Commission staff process employee terminations by the end of the pay period in which an employee leaves service, or in the next pay period. In addition, we recommended CDC maintain a running log of out-of-service employees for comparison to the active payroll register to monitor staff compliance with termination processing standards, and to ensure that out-of-service employees are excluded from CDC's payroll.

In our current review, we reviewed all terminations during calendar year 2003 (approximately 150) and noted that Commission staff entered the effective termination dates within CDC's established guidelines. In addition, we reviewed 10 of these terminations to ensure the employees did not receive inappropriate pay after termination

and noted no exceptions. Further, we noted that CDC staff do not trace the names of terminated employees to the active payroll register to ensure no inappropriate payments are made, as previously recommended.

We also noted two internal control weaknesses related to processing payments for terminated employees. The first weakness occurs as a result of a lag between the employee's effective termination date and the date in which CDC staff inactivate the employee's time and labor capabilities in the personnel/payroll system. The second weakness is the result of staff having certain access to the payroll/personnel system after an employee has terminated. We have discussed the details and the implications of these weaknesses with Commission staff and they stated they could establish the necessary controls within their payroll/personnel system to ensure no inappropriate payments are made.

We consider the recommendation related to processing employee terminations timely to be implemented and the recommendation related to comparing employee terminations to the active payroll register to be not implemented.

CDC management should establish the necessary controls to ensure no inappropriate payments are made after an employee terminates.

Recommendation

- 27. Commission management establish the necessary controls to ensure no inappropriate payments are made after an employee terminates.**

Payroll Distribution

To minimize the likelihood of fraud, payroll warrant distribution controls prohibit a timekeeper's direct involvement in receiving, distributing, storing or otherwise handling payroll warrants. In our original review, we noted that division timekeepers received and distributed payroll warrants. Accordingly, we recommended that only authorized employees with no other payroll, personnel or timekeeping duties assume the responsibility of receiving and distributing payroll warrants and notices of direct deposit. In our current review, we noted that Commission management has assigned the responsibility for receiving and distributing payroll warrants and notices of direct deposit to employees with no other payroll, personnel or timekeeping duties.

We consider the recommendation related to the receiving and distributing of payroll warrants to be implemented.

Payroll Distribution Payoffs

A payroll distribution payoff is a process in which an employee's warrant/direct deposit notice is given to the employee only after the employee has shown proper identification and signed for the warrant/direct deposit notice. In our original review, we noted that

the Commission did not conduct payoffs, nor did it have written procedures requiring payoffs. We recommended Commission management develop and implement payroll distribution payoff procedures and ensure that persons with no other personnel, payroll or timekeeping duties conduct unannounced payoffs, at least annually.

In our current review, we noted that Commission management developed and implemented payroll distribution payoff procedures, and that persons with no other personnel, payroll or timekeeping duties are conducting the payoffs. We also noted that the Commission conducts payoffs generally once each year.

We consider the recommendation related to developing payroll distribution payoff procedures to be implemented.

We also noted that staff conducting the payoffs return unclaimed warrants/direct deposit notices to the payroll section instead of the Financial Management section. Proper internal controls require that unclaimed warrants/direct deposit notices must not be returned to the personnel or payroll sections responsible for original processing. In addition, we noted that the listing employees sign to receive their warrant/direct deposit notice is employee specific, rather than warrant specific. The listing should include all warrants (whether for an active or inactive employee) generated during the pay period, so that CDC staff can detect “ghost” employees or the misappropriation of an inappropriately generated warrant.

Commission management should ensure that warrant distributors return unclaimed warrants/direct deposit notices to the Financial Management section. In addition, Commission management should ensure that the listing employees sign to receive their warrant/direct deposit notice during a payoff is warrant specific, as opposed to employee specific.

Recommendations

Commission management:

- 28. Ensure that warrant distributors return unclaimed warrants/direct deposit notices to the Financial Management section.**
- 29. Ensure that the listing employees sign for their warrant/direct deposit notice during a payoff is warrant specific as opposed to employee specific.**

Workers' Compensation

In our original review, we noted overpayments totaling \$6,800 for eight (53%) of 15 cases selected for review. The overpayments resulted primarily from overlaps between the employees' Temporary Disability (TD) benefits and regular earnings (i.e., vacation, sick). The combined total of an employee's TD benefits and regular earnings should not

exceed 100% of the employee's gross salary. Accordingly, we recommended Commission management monitor employee payroll records in conjunction with reports issued by the third party administrator (TPA) to prevent overlaps in regular wages and TD benefits paid to employees; and seek reimbursement of any overpayments and reinstate the employee's vacation/sick hours.

In our current review, we selected all four workers' compensation cases from FYs 2002-03 and 2003-04 where employees elected to supplement TD income with earned benefit time to determine if any overpayments occurred. We noted that an overpayment of \$305 occurred in one (25%) of the four cases reviewed. However, the overpayment did not occur because the Commission inappropriately supplemented the employees TD income, as was the case in our prior review. The overpayment occurred because Commission staff paid the employee for two holidays while out on leave. Commission's policy is not to pay for holidays while the employee is on temporary disability.

We also noted that CDC staff do not monitor employees' pay records to ensure that employees receiving TD income due to an industrial accident are not inappropriately supplemented with benefit time. CDC needs to monitor employee payroll records in conjunction with reports issued by the TPA to prevent overlaps in regular wages and TD benefits. CDC pursued the collection of overpayments identified during our prior review and was able to collect some of the overpayments.

We consider the recommendation related to monitoring employee payroll records in conjunction with reports issued by the TPA to be not implemented, and the recommendation related to seeking reimbursement to be implemented.

Commission management needs to seek reimbursement of the overpayment identified during our review, and ensure staff are properly trained in coding employees' pay while employees are out on TD leave.

Recommendations

Commission management:

- 30. Pursue collection of the \$305 overpayment.**
- 31. Ensure staff are properly trained in coding employees' pay while out on TD leave.**

Merit Increases

We reviewed the Commission's procedures for awarding annual merit increases to its employees to ensure CDC awards increases in a fair and equitable manner. CDC grants merit increases to its employees based upon the employees' performance rating for the period. For example, supervisors may award salary increases within a specified range for each of the rating categories (i.e., "Meets Requirements", "Exceeds

Requirements”, and “Exceptional”). We reviewed ten employees’ performance evaluations to determine if the merit increases granted aligned with CDC’s merit increase ranges based on the overall rating. We noted no exceptions.

Travel

Commission Travel

Commission employees travel for job related responsibilities such as site visits, professional training, conference attendance, and legislative affairs. In our original review, we noted the Commission needed to strengthen its travel policies and procedures by establishing guidelines for determining the lowest reasonable travel cost, and developing standard procedures for making travel arrangements. The Commission budgeted \$127,644 for travel related expenditures for FY 2003-04.

In our current review, we noted the Commission revised its travel policies to include guidelines for determining the lowest reasonable travel cost. However, we noted CDC still needs to enhance its standard procedures for making travel arrangements, such as providing documentation to support the reasonableness of travel costs.

We consider the recommendation related to the establishment of guidelines for determining the lowest reasonable travel cost to be implemented, and the recommendation related to developing standard procedures to be partially implemented.

Office of Small Business

In 1997, the Board of Supervisors created the Office of Small Business (OSB) in the Community Development Commission to introduce small businesses, generally through contracting workshops, to the economic development initiatives, resources and procurement opportunities available to them throughout Los Angeles County. OSB’s funding consists primarily of County General Fund support. OSB’s FY 2003-04 budget was \$454,000.

Trade Missions

Since 1999, OSB has organized and lead five trade missions to various countries including, Chile, China and South Africa. The total travel costs charged for these five trade missions were approximately \$8,200. Based on a number of communications between CDC staff and the Board, there appears to be some uncertainty regarding the source of funding for these trade missions. For example, in June 1999, the Board encouraged OSB as part of OSB’s responsibility to its Economic Development Association (EDA) grant to assist businesses in expanding their markets to potential clients abroad. In October 1999, OSB notified CDC’s Executive Director that EDA cannot by statute pay for international travel costs. Accordingly, CDC agreed to use County general funds to pay for the trade missions.

We reviewed the trade mission travel expenditures and noted that the South America trip in October 1999 may have been funded by the EDA grant. CDC did not receive the general fund monies until September 2000, at which time the monies were credited to the same account as the EDA grant. As a result, it appears that the trip to South America was paid using EDA funds. CDC should seek direction from the Board to determine if the trade missions should continue with County general funds. In addition, grants and other funding sources should be accounted for separately to ensure only appropriate expenditures are charged against each funding source.

Finally, we noted that OSB does not have formal documented results of the trade missions. The Executive Director of OSB has anecdotal evidence of the outcomes of the trade missions, although she has not formally documented these results to CDC and the Board. To demonstrate the value or benefit of OSB continuing its efforts on these trade missions, CDC management should ensure that OSB formally document the outcomes of the trade missions and report the results to CDC management and the Board.

Recommendations

CDC management:

- 32. Seek direction from the Board to determine if the trade missions should continue with County general funds.**
- 33. Ensure grants and other funding sources are accounted for separately.**
- 34. Formally document the outcomes of the trade missions and report the results to the Board.**

Trade Missions and Other Travel Expenditures

OSB's total travel expenditures for July 1, 2001 through March 2004, inclusive of the trade mission expenditures discussed previously, are \$13,660. We reviewed five trips (64% of the OSB's total travel expenditures) to ensure the costs were reasonable, appropriate, adequately supported and in compliance with CDC's travel policies.

CDC's travel policy and procedures allow employees to claim expenses for meals up to \$55 per day when three meals are purchased in any one day and to claim incidental expenses up to \$58 per day when traveling to specified cities. The policies and procedures do not specifically allow employees to aggregate the amount of expenses claimable over the number of days traveled. An employee can only claim costs he or she incurs on an individual basis per day. In our review of five trips we noted:

- Two (40%) of five trips included meal expenses that exceeded the daily allowed amount. On one trip the expenses claimed exceeded allowed meal expenses by

\$220. On the other trip the expenses exceeded the allowed daily expenses on four days by a total of \$322. It appears that the employee aggregated the expenses claimed over the days traveled to avoid exceeding the total of the daily allowances for the trip.

- OSB's Director took colleagues and/or delegates to lunch and claimed the costs as employee meal expenses which do not fit the definition of meal or incidental expenses.
- One of the two trips discussed above involved travel out of the country. CDC's policy only allows employees to claim incidental expenses when traveling to specified cities, none of which are outside the United States.

CDC management needs to clarify and document its policy for claiming entertainment related expenses. In addition, CDC management should revise its travel policies and procedures to include costs for out of country travel, as deemed appropriate.

CDC's travel policies and procedures require that a travel authorization/advance request be filled out completely including a cost estimate for registration, meals, lodging and transportation and must be approved by an "authorized person" in advance of each trip. One (20%) of five travel authorization/advance request forms did not have the proper approval until the employee returned from the trip. This authorization form also did not have the costs itemized; rather there was one lump sum of money for CDC to advance to the employee.

CDC management should approve travel authorization requests in advance of the trip and require employees to itemize the costs as required by CDC's travel policy.

Recommendations

CDC management:

- 35. Determine expenses employees will be allowed to claim as entertainment related and revise the travel policies and procedures accordingly.**
- 36. Revise its travel policies and procedures to include costs for out of country travel, as appropriate.**
- 37. Properly approve travel authorization forms.**

Loan Programs

City of Industry Loans

Background

CDC receives Redevelopment Housing Set-Aside funds (Industry funds) which consist of 20 percent of the tax increment funds collected by the City of Industry. Per California law and the 1994 Administrative Plan for Industry Housing Funds, the Industry funds must be used for the development of affordable housing within a 15 mile radius of the City of Industry. This area comprises over 60 cities and numerous unincorporated areas and includes portions of the First, Second, Fourth and Fifth Supervisorial Districts.

CDC distributes funds by awarding real estate loans in accordance with the Allocation and Distribution Plan that was approved by the Board of Commissioners on June 2, 1998, and subsequently amended on December 5, 2000. The Board plan included the requirement that 50% of the funds be allocated for affordable housing and 50% for the development of housing for individuals with special needs. As of April 2004, CDC had allocated \$111 million of Industry funds through seven rounds (i.e. an RFP process used to distribute Industry funds) of loan funding beginning in 1998.

CDC uses the RFP process to ensure fair and equitable distribution of funds. CDC hires an outside consultant to evaluate and score proposals from real estate developers. The outside consultant also reviews and responds to developer appeals. An Independent Review Panel (IRP) comprised of individuals who have expertise in real estate, affordable housing lending, housing development and/or supportive services, reviews the consultant's scoring and responses to appeals and decides to accept or to change the scoring. The IRP recommends projects to receive funding to CDC's Executive Director based on the final scoring. The Executive Director then sends a letter to the Board of Commissioners recommending projects for funding. The Board approves the actual funding.

CDC receives Industry loan repayments from developers based on a percentage of the housing development's residual receipts, which essentially equals revenue less expenses on a cash flow basis. CDC uses repaid Industry loan amounts to fund additional Industry loans. Therefore, timely collection of loan repayments increases the amount of funding available for new affordable housing developments.

We reviewed CDC's RFP process for distributing Industry funds to ensure CDC distributed funds in a fair and equitable manner. We also reviewed CDC's procedures for the monitoring of residual receipts to ensure CDC collects allowable loan repayments.

Industry RFP Process

We reviewed the Industry loan RFP and appeals procedures. We also reviewed the consultant scoring and IRP recommendations for the most recent allocation of Industry funds (Round 7). We found the RFP process is executed in a fair, generally consistent and documented manner. However, we noted that CDC can improve the RFP administration and documentation process and the appeals process. For example:

- The evaluation and review of appeals documents did not contain dates and names/or signatures of the individuals completing the evaluation document.
- IRP members did not prepare or sign documentation of the IRP decisions.
- CDC relied on verbal self-reporting of conflicts of interest but did not require consultants or IRP members to sign conflict of interest affidavits.
- CDC only retains proposals from developers who did not receive funding for one year, therefore restricting auditability of the RFP process. CDC should retain proposal and scoring documents for a minimum of five years to maintain auditability of the RFP process.
- CDC did not document the process by which CDC determined the number of points to award two proposers in Round 7 in a departure from the usual scoring procedure. We recalculated the scores and determined CDC awarded the correct number of points.
- The grounds for submitting an appeal are not well defined in the RFP. We noted that many of the issues appealed dealt with information the proposer did not originally include in the proposal. CDC can improve the efficiency of the appeals process by more clearly defining appealable issues in the RFP, including a statement that CDC will not consider new information that was not submitted with the original application.

While the above weaknesses should be addressed to improve the RFP administration, documentation and appeals process, we did not find that the above weaknesses affected the outcome of the RFP process.

Recommendations**Commission management:**

- 38. Require consultants to include the evaluator's name on evaluation documents and responses to appeals, and to sign and date these documents.**

39. **Require members of the IRP to sign and date the IRP meeting minutes indicating approval of the recorded decisions regarding developer proposal scoring.**
40. **Require outside consultants and IRP members to sign conflict of interest affidavits.**
41. **Ensure staff retains proposal and scoring documents, including the developer loan application, for a minimum of five years to maintain auditability of the Industry RFP process.**
42. **Ensure staff thoroughly document departures from the scoring the IRP supplies to CDC's Executive Director, including the method used to determine the number of additional points to award the proposal.**
43. **Clearly define appealable issues in the Industry RFP.**

Industry Loan Repayment Monitoring Process

Developers must pay the lower of the annual loan payment specified in the loan documents or a percentage of the project's prior year residual receipts, which essentially equal rental revenue less operating expenses. If there were no residual receipts in the prior year, the developer does not have to make a loan payment that year. In order to determine the amount of the Industry loan repayment a developer should pay for the year, if any, CDC requires developers to annually submit audited financial statements and a calculation of the prior year's residual receipts. Housing Development and Preservation (HDP) Assets Management staff reviews the financial statements and calculations of residual receipts to verify the reasonableness of the reported residual receipts.

We reviewed HDP Industry loan repayment monitoring files for three projects and noted the following:

- We were unable to determine what steps CDC staff took to review residual receipts because there was insufficient documentation in the files.
- HDP management stated that one of the developers reported higher operating expenses per unit than is standard for FY 2001-02, possibly because the developer included ineligible costs. However, at the time of our review, HDP staff had not followed up to determine whether the developer included only eligible expenses in the calculation of residual receipts.
- In two of three repayment monitoring files we reviewed, the developers did not submit a calculation of residual receipts. We were unable to calculate residual receipts for these two projects because there was insufficient information. In one of these two files, staff noted that there were no residual receipts because the financial

statements showed a net loss. However, it is possible for a project to show a net loss on the financial statements and to still have residual receipts.

- HDP Assets Management staff is responsible for reviewing the developers' financial statements and calculations of residual receipts. HDP staff do not have the expertise in accounting needed to effectively review financial statements and the calculation of residual receipts.
- HDP Assets Management does not have written procedures for monitoring residual receipts in relation to Industry loans.

To ensure adequate monitoring of the Industry loan program, CDC management needs to ensure monitoring files and/or the monitoring database include sufficient documentation; ensure developers submit separate residual receipt calculations; ensure staff with sufficient accounting or financial knowledge review the residual receipt calculations and follow up timely on discrepancies between reported and expected results; consider reviewing all Industry loans to determine if developers correctly reported and paid residual receipts to date, and require developers to pay CDC the required portion of residual receipts, if any; develop and implement written procedures for monitoring Industry loans for residual receipts.

Recommendations

Commission management:

- 44. Ensure monitoring files and/or the monitoring database include sufficient documentation.**
- 45. Ensure developers submit separate residual receipt calculations.**
- 46. Ensure staff with sufficient accounting or financial knowledge review the residual receipt calculations and follow up timely on discrepancies between reported and expected results.**
- 47. Consider reviewing all Industry loans to determine if developers correctly reported and paid residual receipts to date, and require developers to pay CDC the required portion of residual receipts, if any.**
- 48. Develop and implement written procedures for monitoring Industry loans for residual receipts.**

County Business Loan Program

Background

In FY 1992-93, CDC received a \$3 million grant from the Department of Commerce, Economic Development Administration (EDA), to establish the County Business Loan Program (CBLP). The initial purpose of the CBLP was to assist Aerospace or Aerospace related businesses that were adversely affected by federal defense spending, while at the same time experiencing difficulty in obtaining private financing. The EDA required CDC to provide a \$1 million match to supplement the \$3 million grant. CDC used Community Development Block Grant (CDBG) funds to meet the match requirement.

The CBLP is a revolving loan program, where the loan repayments of principal and interest are used by the CDC to fund new loans. Under EDA guidelines, once CDC loaned out the initial \$4 million, the EDA no longer required the loans to be used for businesses impacted by Aerospace downsizing. CDC could loan funds to other businesses unable to obtain private financing.

Since the program's inception, CDC has awarded 49 loans totaling approximately \$12.2 million. CDC staff prescreen loan applicants for eligibility under EDA and/or CDBG guidelines, and then evaluate loan applicants for their ability to repay the loan. CDC staff recommend applicants for funding to the CBLP Loan committee (committee), comprised of seven individuals (two from CDC, three from private lending institutions, and two from the Business community) appointed by CDC's Executive Director. The committee is responsible for reviewing and approving loan applications, recommending loan policy to CDC's Executive Director, and making final decisions concerning CBLP loans.

We reviewed CDC's loan approval process to determine if CDC awards loans in a fair, accurate and appropriate manner to minimize the risk of loss. We also reviewed CDC's procedures for monitoring loan repayments to ensure CDC collects repayments timely. Overall, we noted that CDC's default rate of 2% for the CBLP compares favorably with other government funded loan programs which have default rates ranging from 23% to 44%.

Business Administration Plan

CDC has a Business Administration Plan (Plan) detailing the policies and procedures of the CBLP. The EDA approved CDC's latest revised Plan in April 1997. However, we noted CDC can revise/update its Plan to reflect current business practices. For example, the Plan does not address the following:

- The types of businesses (i.e., other than Aerospace) that are eligible to receive loans.

- The requirements unique or specific to the CDBG program. For example, under both EDA and CDBG guidelines, loan applicants are required to create one job for every \$35,000 loaned. However, the CDBG program also requires that 51% or more of the jobs created be for low to moderate income families. In addition, the CDBG program requires the business be in the Los Angeles Urban County jurisdiction which includes unincorporated areas and 48 cities that participate in the County's CDBG program.
- CDC's practice requiring businesses to provide financial statements on a pre-determined basis (i.e., quarterly, annually), and the types of analyses CDC staff perform to determine an entity's continued ability to meet its financial obligations under the loan.
- CDC's practice requiring businesses to provide proof of hazard and liability insurance annually.

CDC management needs to update its CBLP Plan to ensure procedures reflect current operating practices and requirements. Once revised, CDC should submit its revised Plan to the EDA for approval.

Recommendation

- 49. CDC management update the CBLP Plan to reflect CDC's current business practices and obtain EDA Approval.**

Compliance with Business Administration Plan

We selected three loans (i.e., one past due, one current, and one that CDC had charged off) funded by the CBLP to determine if CDC complied with its Business Administration Plan in awarding the loans. We noted areas where CDC can improve its compliance with the Plan, as follows:

- One (33%) of three applicants did not submit a business plan with financial projections indicating the business' future fiscal viability. In addition, the applicant did not submit personal tax returns. Under the CBLP, applicants can be held personally liable for failure to repay the loan.
- One (33%) of three applicants did not submit an accounts receivable aging or a schedule of debt including outstanding balances, repayment schedules, and due dates.

The Plan also requires the loan officer to prepare a credit memorandum for the Loan committee summarizing the recommended loan transaction. CDC's Plan details the information to be included in the credit memorandum in order for the committee to make its decision. We noted instances in which CDC staff did not include all required information in the credit memorandum, as follows:

- Two (67%) of three credit memorandums did not contain a statement indicating that the applicant was unable to obtain private financing, a requirement of the CBLP. In addition, in one (50%) of the two instances, there was no documentation in the loan file substantiating the applicants' inability to obtain private financing.
- One (33%) of three credit memorandums reviewed was lacking an estimate of the business' future projected earnings.

To ensure loans are awarded in a fair and equitable manner, CDC management needs to ensure loan files and data supplied to the Loan committee for decision making purposes is complete and in compliance with the Plan. Departures from current policy should be documented and justified in the applicant's loan file.

Recommendation

50. CDC management ensure loan files and data supplied to the Loan committee is complete and in compliance with the Plan. Departures from current policy should be documented and justified in the applicant's loan file.

Monitoring Process

We evaluated CDC's monitoring efforts for the three loan files reviewed and noted the following:

- Two (67%) of three loan files did not contain proof that the jobs created condition (i.e., one job created for every \$35,000 loaned) was met. Although CDC made numerous attempts to obtain the information, there was nothing documented in the loan file at the time of our review to indicate the businesses ultimately fulfilled this requirement.
- One (33%) of three loan files did not submit all financial statements as required. As previously stated, businesses are required to submit financial statements in order for CDC staff to evaluate the businesses' continued ability to meet its financial obligations under the loan.
- For all three (100%) of the loans reviewed, CDC staff did not document financial statement analyses in the loan files. CDC's current practice requires staff to conduct financial analyses to determine whether the business will be able to meet its repayment obligations under the loan.
- In two (67%) of three loan files reviewed, CDC staff did not have current proof of hazard and liability insurance.
- In one (33%) of three loan files reviewed, CDC did not initiate legal action for approximately three years from the date the business became delinquent. Although

CDC contacted the business on numerous occasions, CDC's Plan requires they contact legal counsel to initiate collection efforts 90 days after the original delinquency.

Recommendations**CDC management:**

- 51. Ensure loan files contain sufficient documentation to indicate that loan requirements (i.e., jobs created condition) have been met.**
- 52. Ensure staff conduct and document financial analyses to determine a business' ability to meet its future financial obligations under the loan.**
- 53. Require staff to annually obtain and review proof of each business' hazard and liability insurance.**
- 54. Initiate action on delinquent loans in a timely manner.**

Status of Recommendations - May 2000 Fiscal Review

Reco #	Audit Area	Current Status
2	Budgetary Controls	Partially Implemented
3	Budgetary Controls	Implemented
14a	Procurement	Partially Implemented
14b	Procurement	Not Implemented
14c	Procurement	Not Implemented
15a	Procurement	Implemented
15b	Procurement	Partially Implemented
16a	Procurement	Not Implemented
16b	Procurement	Not Implemented
16c	Procurement	Not Implemented
17	Procurement	Implemented
18	Procurement	Partially Implemented
19	Procurement	Not Implemented
20	Contracting	Implemented
21a	Contracting	Partially Implemented
21b	Contracting	Implemented
22a	Contracting	Not Implemented
22b	Contracting	Partially Implemented
23a	Contracting	Not Implemented
24a	Contracting	Implemented
24b	Contracting	Implemented
25	Contracting	Partially Implemented
26a	Contracting	Implemented
26b	Contracting	Partially Implemented
27a.	Personnel and Payroll	Implemented
27b.	Personnel and Payroll	Partially Implemented
28a.	Personnel and Payroll	Implemented
28b.	Personnel and Payroll	Implemented
29a.	Personnel and Payroll	Implemented
29b.	Personnel and Payroll	Implemented
30a.	Personnel and Payroll	Implemented
30b.	Personnel and Payroll	Not Implemented
31	Personnel and Payroll	Implemented
32	Personnel and Payroll	Implemented
33a.	Personnel and Payroll	Not Implemented
33b.	Personnel and Payroll	Implemented
46a.	Travel	Implemented
46b.	Travel	Partially Implemented

Community Development Commission

February 22, 2005

To: J. Tyler McCauley, Auditor Controller

From: Carlos Jackson, Executive Director

SUBJECT: RESPONSE TO AUDITOR CONTROLLER FISCAL REVIEW

Attached is the Commission's response to the Auditor Controller's draft Fiscal Review dated January 2005. I appreciate the review conducted by your office and the various recommendations to enhance our operations. Furthermore, you will notice on some of the findings that we have already instituted corrective actions to mitigate the circumstances and their findings. In general, we agree with the findings contained in the report, however, there are some areas in which we have a different perspective. In those areas of disagreement, we have provided the bases for our points of view.

I would like to note that the differences in our points of view stem primarily from the fact that the Commission is a separate legal entity outside of the County family structure, therefore, we have had to develop our own general policies and procedures. As you know, the Commission, as requested by the Board dating back to 1982-83, has developed its own administrative systems, such as, separate personnel policies, payroll system, and budgetary controls. To highlight this, Commission employees are under the California Public Employees Retirement System (PERS) and not LACERA (Los Angeles County Employees Retirement Association). In addition, the Commission's budget is submitted separately from the County's annual budget and must be approved by our Commissioners by July 1st in order for the various federal programs to be funded.

In reference to the budget amendment authorization finding, I would like to state that I take exception to the implication of this finding. As a result of your May 2000 fiscal review of the Commission, you requested that we seek a Board policy governing our budget amendments. As requested, we had the Board adopt such a policy, which your office reviewed, in draft, prior to the Board's approval. Your current finding implies we did not at that time fully disclose to the Board the issue identified. After reviewing the draft policy issue, if you had instructed us to consider this as well, we would have done so. It is unfortunate for both our agencies that we did not consider this item in May 2000.

With the exception of the budget matter, I sincerely appreciate your staff's professionalism and courtesy in conducting this review. Their observations and comments have helped us enhance our administrative operations.

CJ:sm
Attachment

RECOMMENDATIONS AND RESPONSES
TO DRAFT AUDIT REPORT - 2004 FISCAL REVIEW

BUDGETARY CONTROLS

Budget Amendment Authorizations

1. **RECOMMENDATION:** Commission management clarify with the Board whether or not the Board intended to grant CDC's Executive Director *unlimited* budget adjustment authority.

RESPONSE: In the previous audit, a 1994 budget policy was used to justify the Commission's budget amendments; however, no formal Board approval could be located. Based on the recommendation contained in the Auditor-Controller's findings in 1999, the Commission submitted a request to the Board to authorize the Executive Director to transfer appropriations between expenditure types within the same budget unit. This request was reviewed by the Auditor-Controller prior to the approval of your Board in June 2000.

Since the Executive Director is required to obtain Board approval for all contracts exceeding \$49,999, the Commission's current practice does not pose financial risk to the Commission or the County. Furthermore, the Commission's control system tracks funds by account and project, and no division can exceed the authorized amounts due to these expenditure controls.

The Commission maintains full control over budgetary expenditures, because expenditures cannot be generated unless sufficient budget is available. Specifically, as funds are awarded or received, the Commission incorporates additional budget authority through the Board approval process.

In contrast, County departments notify the CAO and the Auditor-Controller's Accounting Division of all budget adjustments, regardless of the amount, in order to ensure the availability of funds and accurate reporting of departmental final adjusted budgets.

During previous discussions with the CAO Budget Analyst, it was acknowledged that it would not be possible for the CAO to track adjustments or verify fund availability, because the Commission does not utilize CAPS and its funding is from HUD. Therefore, submission of budget amendments would serve no purpose.

It should be noted that during the last fiscal year, the Commission processed a substantial number of budget amendments without having divisions exceed the

authorized amounts. It should also be noted that the Auditor-Controller's report cites no cases of neglect or misappropriation of funds under the current system. Independent audit reviews also indicate that the Commission is fully accountable for the use of its funds.

Budget Administration

2. **RECOMMENDATION:** In conjunction with the CAO, establish procedures to annually report its final adjusted budget to the CAO for inclusion in the official Final County Budget.

RESPONSE: In prior submissions to the CAO, it was agreed that the Commission would not submit adjusted budget numbers, since the CAO did not review or approve the Commission's budget adjustments. For Fiscal Year 2003-2004, the Commission in conjunction with the CAO, reported its final adjusted budget for inclusion in the County's Final Budget Book at the recommendation of the Auditor-Controller. The Commission recommends continuing this practice.

3. **RECOMMENDATION:** Ensure its internally generated budget book reflects the correct annual final budget.

RESPONSE: Unlike the County, HUD requires that the Commission submit its budget to the Board by July 1st of each year to ensure that program funds are available. Therefore, the Commission's Fiscal Year is completed after submission of its budget, making it impossible to incorporate final adjusted budget numbers into the published Budget Book. While the County publishes a preliminary and a final budget book, the Commission only publishes the final version that is completed prior to the end of the Fiscal Year. The final adjusted budget is always reported in the year-end component of the Comprehensive Annual Financial Report prepared by the Financial Management Division in conjunction with the Commission's external auditors.

Capital Projects

4. **RECOMMENDATION:** Seek Board approval to shift funds between or among separate capital projects and/or budget units.

RESPONSE: The Auditor-Controller states that all County departments must establish a separate budget unit for each capital project. However, as noted in the introduction to this response, the Commission utilizes systems that conform to the requirements of its funding sources, which are markedly different from those of the County.

The currently policy was established in conjunction with the Auditor-Controller, and at the time of implementation no request was made to require separate budget units. However, the Commission will amend the Capital Budget Policy to require Board approval to shift funds between separate budget units for each capital project.

5. **RECOMMENDATION:** Evaluate and document the feasibility of establishing separate budget units for its capital projects through its existing PeopleSoft accounting system.

RESPONSE: For Fiscal Year 2004-2005, the Commission has only four capital projects, at a total cost of \$3.05 million, which is less than one percent of the total budget. It seems unreasonable to invest funds to modify the accounting and budget systems, when the impact on the overall agency would be minimal, versus the cost and labor that would be required for the modifications.

In addition, the Government Code leaves it to the discretion of the Board of Commissioners to develop policies for capital projects. Given the fact that the Commission is 90 percent federally funded, and is in full compliance with all HUD guidelines, this does not seem to be a practical option for the Commission to undertake, given the recent cuts in federal revenues the Commission receives.

Encumbrance Accounting

6. **RECOMMENDATION:** Commission management encumber the full amount of contracts (or other binding legal obligations) upon execution.

RESPONSE: We disagree with the audit finding because the contract feature of PeopleSoft supersedes the encumbrance aspect. Furthermore, the report overlooks the *contract* feature of the PeopleSoft financial system. For example, when a contract is executed, the full value of the contract is set up on the *contract* function within the financial system. For each fiscal period, the *Encumbrance Orders* are then set up to match the respective period's purchases per the applicable contract. The systems *contract* feature then serves as a controlling tool to prevent the over-committing of purchases beyond what is allowed in a contract, irrelevant of the contract period, single or multi-year.

The *Encumbrance Orders* serve as the guiding tool to ensure that spending does not exceed the fiscal year's budget. Since *Encumbrance Orders*, like Purchase Orders, are interactive with the annual budget appropriation at the project/cost center and object code level, it enables management to maintain expenditures at the line-item level.

Moreover, the encumbrance function in the Commission's financial system is two tiered. First, at the contract level, the system contract function monitors the full value of a contract throughout the life of the contract. Second, during each fiscal year, the ***Encumbrance Orders*** control the spending of each procurement commitment for a particular contract so as not to exceed that year's budget, and cumulatively, not to exceed the life-to-date total of the contract.

As for the Auditor-Controller's concern that the Commission will not be able to meet its legal (contractual) obligations should funding become exhausted, it should be noted that all of the Commission's contracts (even multi-year contracts) are funded on an annual basis, based on funding and performance. Furthermore, contracts contain specific language not committing the Commission or the County financially in the event that funding is not available.

Administrative Policies and Procedures Update

7. **RECOMMENDATION:** Commission management update its Administrative Policies and Procedures to reflect its unanticipated revenue procedures and other current budgetary and accounting practices.

RESPONSE: The Commission does not have a budgetary policy on revenue recognition included in its Administrative Policies Procedures. The Commission follows accounting procedures and practices in accordance with the applicable standards established by the Governmental Accounting Standards Board. The existing policy on budget amendment from 1984 will be updated and amended following Board direction on the outcome of the audit findings.

Budget Status Reports

8. **RECOMMENDATION:** Commission management develop and implement a policy requiring division staff to complete budget status reports on a consistent basis (i.e., quarterly) and to submit the reports to the Executive Office of Budget for review.

RESPONSE: The Commission has implemented a quarterly review as part of its Strategic Planning Process. All reports for the first and second quarters of Fiscal Year 2004-2005 have been received and reviewed by the budget department in consultation with the Executive Director.

ADHERENCE TO CDC BUDGET

9. **RECOMMENDATION:** Commission management re-evaluate the method used to present its revenue budget for City of Industry funds in its accounting records and financial reports to better reflect their budgeted financial position.

RESPONSE: The Commission's expenditure ratios for the 2002-2003 and 2003-2004 were 88% and 96%, respectively, which are excellent ratios. In comparison, the County's achieved an expenditure ratio of 74% for 2002-2003.

With regard to the revenue variances for the City of Industry, this was previously discussed with the Auditor-Controller during the audit. The variance is due to the fact that according to State guidelines, revenue from the City of Industry is recognized as received. Given the fact that the development of housing is a multi-year activity, the Commission will never be exact in determining revenues and expenditures for City of Industry funds. Since the Commission is not permitted to present a budget that is not balanced, the result is current budget variances will continue since the revenue received will always be recognized in the current Fiscal Year, whereas expenditures will be included as needed.

PROCUREMENT

Purchase Order Changes

The report states: "We consider the recommendation related to CDC revising its Purchasing Policies and Procedures Manual to be not implemented, and the recommendation related to complying with established change order procedures to be partially implemented." Clarification is requested regarding whether the Commission is being asked to complete these two actions, since no formal recommendations were provided.

Solicitation of Quotations

10. **RECOMMENDATION:** Commission management ensure staff document at least three price quotations for purchases between \$1,000 and \$24,999 and document its procedures in its Purchasing Manual.

RESPONSE: The Auditor-Controller's report acknowledges that this recommendation has been implemented, but mistakenly states that it is not included in the Purchasing Policies and Procedures Manual. In fact, it is included in *Section III – 2, Small Informal Purchase Procedures*. Although the current

procedure does not require the divisions to submit documented bid information on the requisition form, it does require divisions to maintain all of the price quotation information internally.

In order to ensure that all bid documentation is maintained in a centralized file, the Commission will begin requiring divisions to submit this documentation with all purchase requisitions by April 1, 2005.

Matching Payment Documents

11. **RECOMMENDATION:** CDC management clarify its policies for acknowledging and documenting the receipt of goods and services.

RESPONSE: A procedure for acknowledging and documenting the receipt of goods and services has been partially implemented. By May 18, 2005, an internal policy will be implemented and the Procurement Procedures Manual will be amended to ensure that persons ordering items do not also sign the related invoice acknowledging receipt. In addition, Accounts Payable will not process payment without an authorized signature on the invoice. Training will be provided, as necessary.

Timeliness of Payments

12. **RECOMMENDATION:** Ensure staff pay invoices within the required time frames.

RESPONSE: We disagree with the Auditor-Controller's methodology for determining the timeliness of payments, because it is based on calculating the number of days past due by comparing the invoice date, plus one week, to the date paid. Based on the Auditor-Controller's methodology, only one week is allowed for the Commission to pay its vendors. Most of the Commission's vendor invoices have a 30-day term (net 30 days). A time frame of 30 days from invoice date would be more appropriate for such testing.

The Commission's policy requires that approved and documented invoices be paid on time (by the due date). Most invoices have a 30-day term and no discounts. The Commission's goal is to pay each vendor by the agreed-upon due date.

13. **RECOMMENDATION:** Require Division staff to date stamp invoices upon receipt.

RESPONSE: By March 31, 2005, the Commission will implement a procedure to ensure that on a daily basis staff date stamps invoices upon receipt. The Receiving and Handling Policy will be updated to include this procedure.

Blanket Purchase Orders

14. **RECOMMENDATION:** Work with the Los Angeles County ISD regarding the proper utilization of BPOs.

RESPONSE: On July 7, 2004, the Commission's purchasing staff met with Tom McKee from ISD to discuss the BPO process that the County uses to obtain common-use items and/or services.

15. **RECOMMENDATION:** In conjunction with ISD, if appropriate, evaluate its system capabilities for establishing a "sub-order" system for monitoring and controlling BPO-related expenditures.

RESPONSE: The BPO model is used by the County to purchase enormous quantities of goods and services for use Countywide. This is appropriate to the County's needs because of the costs savings resulting from discounts that are realized when purchasing in large volumes.

In contrast, the Commission's purchases are miniscule compared to the bulk purchasing conducted by ISD for the County. During this fiscal year, the Commission implemented the Master Contracts System, which is similar to the County's Blanket Purchase Order (BPO) system and sub-order system for monitoring and controlling expenditures. The Board has already approved contract awards under this system, including demolition services on January 17, 2004 and appraisal services on October 12, 2004. In addition, the Board is scheduled to approve a contract for asbestos abatement services on February 8, 2005, also procured under the current system.

The Master Contracts System was implemented for certain goods and services to eliminate the need to conduct separate Requests for Proposals (RFP) for each division. The system starts after vendor selections are made and Master Contracts are issued for the various vendors. As divisions begin use of services and commodities, an Encumbrance Release Order for payment is prepared which is tied to a specific Master Contract, similar to the BPO system. In this manner, costs are controlled, because expenditures cannot exceed the amounts allocated under the Master Contracts.

The Commission only uses the BPO model on a very limited basis for the purchase of Commission-wide goods and services that it anticipates will be needed throughout the year. In such cases, bulk purchasing is appropriate. However, sole use of the BPO model would not be cost effective or practical because: unlike the County, there is not sufficient need for large quantity purchases; significant cost savings would not be achieved due to lack of volume; there is insufficient physical space to warehouse large quantities of items; staff resources are not available to monitor such a large system Commission-wide; and total conversion to the BPO model would require costly changes to the electronic monitoring systems that would not be off-set by any cost savings.

Furthermore, a very similar model to the BPO was previously tested and resulted in reduced efficiencies and greater costs to the divisions for goods and services. Because of the large purchases previously made under this model, some parts and products were not moving from the warehouse to the divisions fast enough, and parts became obsolete. Vendors would not allow trade-backs for newer parts, resulting in a loss for the Commission.

As recommended, the Commission has evaluated implementation of the BPO model agency-wide, and has determined that the Master Contracts System is the most “appropriate” model to meet its needs. The Master Contract System is currently part of the Commission’s pilot program for the centralization of procurement systems.

CONTRACTING

Unless otherwise noted, the procedural changes related to Recommendations 16 through 23 will be implemented by May 18, 2005.

Solicitation Documents

- 16. RECOMMENDATION:** Ensure that the evaluation documents fully disclose the purpose of the oral interview.

RESPONSE: The Commission’s solicitation documents state that interviews *may* be conducted to gather details regarding specific experience, qualifications and other relevant information. The Central Services Unit will assist staff when the solicitation package is being developed to ensure that intent of the oral interview is fully disclosed. This information will be included in the Commission’s solicitation package.

17. **RECOMMENDATION:** Require proposers to provide all the necessary documentations (e.g., certifications, licenses, etc.).

RESPONSE: The Commission previously required that proposers indicate in their RFP responses whether they hold the necessary certifications, licenses, etc. Although copies of the documents were not required as part of the response, staff was instructed to verify good standing on appropriate Internet sites.

The Commission now requires that copies of these documents be provided by the proposers as part of their responses. This procedure will be included in the Purchasing Procedures Manual and solicitation documents that are currently being updated for implementation by September 1, 2005. Appropriate agency-wide training will also be conducted.

18. **RECOMMENDATION:** Include relevant and significant minimum requirements in the RFP.

RESPONSE: By May 18, 2005, clarifying language will be added to the RFP solicitation documents and to the amended Procurement Procedures Manual, and staff will be provided with appropriate training. It should be noted that line divisions conduct many of their own procurements due to the limited resources of the Central Services Unit. Unlike ISD, the Commission does not have the resources to implement a fully centralized procurement unit where *all* procurements can be conducted.

The Commission relies on the divisions to conduct their own informal procurements. The Central Services Unit provides the divisions with training and guidance on developing thorough solicitation documents. The Procurement Procedures Manual is currently being updated to include this and other related information. The Commission will continue to utilize tools such as the Internet and regular training sessions to ensure that staff has the information necessary to prepare solicitation documents, and will review a sampling of RFP's for quality control purposes to ensure they contain relevant and significant minimum requirements.

Proposal Evaluation Instrument

The report states: "We consider our recommendation related to providing evaluators with sufficient space to document how they arrived at their scores as not implemented." Clarification is being requested regarding whether the Auditor-Controller is asking for completion of this action, since no formal recommendation was provided.

19. **RECOMMENDATION:** Commission management ensure that the questions on the evaluation instrument address the distinct functions being evaluated.

RESPONSE: The Central Services Unit will implement a sample evaluation document that will incorporate the evaluation criteria and process. The Training and technical assistance will be provided to ensure that the evaluation instrument addresses the distinct functions being evaluated.

Evaluation Process

The report states: “We consider our recommendation related to requiring evaluators to meet and compare and summarize the evaluations and documenting the committee’s selection process as not implemented.” Clarification is being requested of the Auditor-Controller regarding whether action is requested, since no formal recommendation was provided.

20. **RECOMMENDATION:** Ensure that panel members sign conflict of interest affidavits or certifications prior to evaluating proposals.

RESPONSE: Some divisions have already implemented the new *Certification of No Conflict of Interest* form for solicitations that contain an evaluation instrument, and require evaluators to sign a copy prior to evaluating proposals. This procedure is currently being implemented Commission-wide.

21. **RECOMMENDATION:** Ensure an appropriate mix of program and non-program staff comprise evaluation teams.

RESPONSE: The Commission’s position is that employees directly involved with the program are best suited and have the necessary expertise and program experience to properly evaluate proposals under consideration. Therefore, the Commission includes non-program staff as part of its evaluation teams to the extent that outside expertise is required to ensure comprehensive evaluations.

While the Auditor-Controller acknowledges that technical expertise is important, the report emphasizes that “perceptions” of impropriety could arise if the evaluation panel consists mainly of program staff. However, the Commission has a structured appeals process in place to respond to proposers who feel that an evaluation was not conducted fairly. This process is used to fully explain the evaluation and solicitation process. The Commission believes that the current practice, along with the established appeals process, is more than adequate to address any perceptions of impropriety.

22. **RECOMMENDATION:** Establish guidelines for determining the appropriate weight and specific criteria for evaluating references.

RESPONSE: Two members of the Purchasing Unit attended and completed the County's 100-hour Procurement and Contracting training course. As a result, the Commission has implemented on a limited number of the County's practices for determining the appropriate weight and criteria for evaluating references. The guidelines will be delineated in the Procurement Procedures Manual.

Unlike ISD, the Commission's procurement functions are not fully centralized. Various divisions often conduct their own informal procurements, with the assistance of the Central Services Unit which provides tools through the Intranet, regular staff training, standard documents and forms and other assistance related to RFP development and management. The Central Services Unit will continue assisting staff and sampling RFP documents to ensure that the Commission's established standards are met. The Commission views this as the most appropriate arrangement, based on available resources.

23. **RECOMMENDATION:** Commission management ensure that staff document the scoring methodology and maintain documentation to support their conclusions in the contracting file.

RESPONSE: The Commission has implemented the County's practices for documenting the scoring methodology and is maintaining documentation to support conclusions in the contracting file. The guidelines will be delineated in the Procurement Procedures Manual.

REQUESTS FOR PROPOSALS/QUALIFICATIONS (RFP/RFQ)

Disclosures

24. **RECOMMENDATION:** Commission management ensure Division staff utilize the procurement folder to access standard disclosures and language for solicitation documents.

RESPONSE: A Procurement Folder is currently available in the Commission's Common Directory to assist staff use in developing solicitation documents. In order to broaden use of this information, the Commission is developing a comprehensive Central Services Intranet Web Page that will be included on the Commission's Intranet Home Page. The new, more user-friendly Intranet Web Page will be completed by September 1, 2005. In the interim, regular

announcements will be sent to staff to remind them to access the current folder to obtain the latest disclosures and standard language for solicitation documents.

25. **RECOMMENDATION:** Commission management ensure staff documents in the meeting minutes discussions and conclusions reached at the bid opening process.

RESPONSE: The Commission will continue to use the Record of Bid Opening document. In addition, instructions will be provided to all divisions to include in the meeting minutes a summary of all discussions and conclusions reached during the bid opening process. These instructions will be included in formal staff training and in the Purchasing Policies and Procedures Manual.

PERSONNEL AND PAYROLL

Bilingual Bonus/Authorization

26. **RECOMMENDATION:** Commission management identify and re-test all employees receiving bilingual compensation that do not have proof of successful completion of the bilingual proficiency examination from the testing agency in their personnel file.

RESPONSE: The Commission has identified and retested all individuals who are currently receiving the benefit and who did not have proof of successful completion of a bilingual proficiency examination in their personnel files. A total of 32 employees were retested and passed, and the examination results have been included in their personnel files.

Employee Terminations

27. **RECOMMENDATION:** Commission management establish the necessary controls to ensure no inappropriate payments are made after an employee terminates.

RESPONSE: Currently, Human Resources checks terminated employees against the active payroll system to ensure that no inappropriate payments are made. In the future, Human Resources will create a new “system” within payroll, which will include only terminated employees. Only designated Human Resources staff will have access to the system, thereby prohibiting unauthorized persons from entering hours for any terminated employees. This procedure will be fully implemented by March 31, 2005.

Currently, the Payroll Section verifies that a terminated employee is not on the active payroll register.

Payroll Distribution/Payoffs

- 28. RECOMMENDATION:** Ensure that warrant distributors return unclaimed warrants/direct deposit notices to the Financial Management section.

RESPONSE: Commission management has changed its procedures to ensure that warrant distributors return unclaimed warrants/direct deposit notices to the Internal Control staff. This will be implemented in the next payroll distribution payoff.

- 29. RECOMMENDATION:** Ensure that the listing employees sign for their warrant/direct deposit notice during a payoff is warrant specific as opposed to employee specific.

RESPONSE: This recommendation will be implemented in the next payroll distribution payoff. The listing which employees sign for their warrant/direct deposit notice during a payoff includes not only the warrant or deposit notice number issued, but will also the employees who received any payment at all from the department during the entire year. This process not only accounts for every warrant that is issued on that day, but also accounts for every payee during the entire year. Commission management believes that this process is the only way to flush out any illicit activities for an entire 12-month period.

Workers' Compensation

- 30. RECOMMENDATION:** Pursue collection of the \$305 overpayment.

RESPONSE: The \$305 overpayment will be deducted from the employee's permanent disability award settlement.

- 31. RECOMMENDATION:** Ensure staff are properly trained in coding employees' pay while out on TD leave.

RESPONSE: The Risk Management Safety Analyst is currently verifying timecards for all employees who are receiving Temporary Total Disability benefits. In addition, additional training is being provided to division timekeepers to ensure that they are properly coding timecards for impacted employees.

TRAVEL

Commission Travel

The report notes that the recommendation for developing standard procedures is partially implemented, and that the Commission “still needs to enhance its standard procedures for making travel arrangements, such as providing documentation to support the reasonableness of travel costs.”

The Commission’s travel policy currently includes parameters for determining the “lowest logical airfare available.” Staff is also required to print, at a minimum, three price quotes from the various Internet travel sites to support the reasonableness of travel costs. An updated travel policy will be published by April 2005, and will include the three-price quote requirement, as well as other procedural clarifications.

Office of Small Business/Trade Missions

On January 4, 2005, the Board has approved the transfer of the Office of Small Business (OSB) to the Internal Services Division (ISD). Therefore, Recommendations 32, 33 and 34 will be referred to ISD for consideration.

Trade Missions and Other Travel Expenditures

- 35. RECOMMENDATION:** Determine expenses employees will be allowed to claim as entertainment related and revise the travel policies and procedures accordingly.

RESPONSE: The Commission’s policies will be amended to define under what circumstances employees can pay for meals and other expenses for business associates. The new language will be included in a revised policy to be released by April 2005.

- 36. RECOMMENDATION:** Revise its travel policies and procedures to include costs for out of country travel, as appropriate.

RESPONSE: The Commission will not authorize any out of country travel without Board approval.

37. **RECOMMENDATION:** Properly approve travel authorization forms.

RESPONSE: The Commission has procedures in place to ensure that travel advance forms are only approved when detailed travel information is provided. These procedures will continue to be carefully monitored.

LOAN PROGRAMS - CITY OF INDUSTRY

Industry RFP Process

38. **RECOMMENDATION:** Require consultants to include the evaluator's name on evaluation documents and responses to appeals, and to sign and date these documents.

RESPONSE: Previously, the Commission maintained notes to record which consultant evaluated each project, however, new evaluation forms have been developed and implemented that include the evaluator's name, date and signature.

39. **RECOMMENDATION:** Require members of the IRP to sign and date the IRP meeting minutes indicating approval of the recorded decisions regarding developer proposal scoring.

RESPONSE: Previously, staff prepared a memo to file documenting the IRP meetings. Now IRP members are required to sign and date their approval of IRP meeting minutes.

40. **RECOMMENDATION:** Require outside consultants and IRP members to sign conflict of interest affidavits.

RESPONSE: Please see the response to Recommendation No. 20.

41. **RECOMMENDATION:** Ensure staff retains proposal and scoring documents, including the developer loan application, for a minimum of five years to maintain auditability of the Industry RFP process.

RESPONSE: The Commission currently keeps unfunded binders for one year, and has not had the need to retrieve information from an unfunded application and not having it available. Developers have the right to appeal a denied application to the IRP, the Executive Director and the Board of Supervisors, therefore, any disagreements are dealt with quickly and thoroughly using the Commission's current process. Additionally, all proposals are time sensitive and typically have multiple funding sources that, if not funded within one or two years, are lost.

Furthermore, it is generally not feasible to Laserfiche or store these voluminous documents which typically include divider sheets and some oversized pages. Therefore, if a proposal is denied, we will continue to maintain it for one year. Retaining un-funded applications for a longer period would put undue pressure on an already overburdened storage system. Furthermore, there is no legal requirement or substantial purpose in retaining proposals beyond the timeframe currently employed by the Commission.

42. **RECOMMENDATION:** Ensure staff thoroughly document departures from the scoring the IRP supplies to CDC's Executive Director, including the method used to determine the number of additional points to award the proposal.

RESPONSE: The Board is advised of any departures from the IRP scoring in memoranda that precede the filing of the Board letter requesting approval of the award recommendations. The reasons for overriding an IRP recommendation or awarding additional points are fully disclosed in the memoranda and the Board letter.

Internally, the Commission will thoroughly document reasons for any departures from the usual scoring process that the IRP supplies to the Executive Director. In the specific case noted by the Auditor, the departure was the awarding of additional points to developers who made a minor error that normally would not have been awarded. However, in that round (Round 7) the funding was, for the first time, under subscribed (i.e., there was more money available than requests for funding). As a result, the decision was made to reinstate the points removed for the minor error so that the remaining funds could be awarded to a badly needed affordable housing development. The IRP agreed with this decision and the Board of Supervisors was made fully aware of the matter in the Round 7 Board letter.

43. **RECOMMENDATION:** Clearly define appealable issues in the Industry RFP.

RESPONSE: The most recent Industry RFP (Round 8) and the initial scoring letter to the developers contained clarifying language concerning appealable items. However, the Commission does not believe the number of appeals will be significantly reduced. The Industry RFP process is often highly competitive. Additionally, the applicant's scores are not made available to other applicants until the funding allocations are finalized. Therefore, developers have, and will continue to, appeal any item, appealable or not, in an attempt to get additional points. In the past, even projects that have scored very high have appealed. The large number of appeals is attributed primarily to the competitive nature of the RFP process, and not to the quality of the technical reviews or the RFP itself.

Industry Loan Repayment Monitoring Process

44. **RECOMMENDATION:** Ensure monitoring files and/or the monitoring database include sufficient documentation.

RESPONSE: Typically, most affordable housing developments do not produce excess cash (i.e. residual receipts). This is because the initial underwriting of these developments provides only the assistance necessary to construct the project and possibly build-up operating and replacement reserves over time that would ultimately be used for the project. There is also a lack of excess cash since the rents, which are used to operate and maintain the property, are initially set at below-market levels and are subsequently limited to annual adjustments that are based on an increase in area median income, which can be half as much as the increase in project expenses, which will increase at the higher “market level” rate. Therefore, the primary goal of the Commission’s housing development and preservation function is to accomplish its mission of effectively using resources to provide affordable housing while exercising an industry-standard of due diligence in the monitoring and enforcement of residual receipt loans and of tenant eligibility, affordable rents and housing quality standards.

While we continue to strengthen our tracking and monitoring techniques through the experience gained as a major affordable housing producer, the cost-benefit considerations of any action taken in these areas is of primary concern. It is, therefore, generally not advisable to take monitoring or enforcement action with respect to residual receipts that will cost significantly more than is like to be recovered from projects that typically have limited cash flows.

The Commission has established Asset Management Policies and Procedures to describe its cost-benefit approach to evaluating and enforcing residual receipts, a Residual Receipt Calculation Detail (RRCD) form, and screen shots of the enhanced tracking systems utilized by the Housing Development and Preservation Division. We have incorporated into the RRCD form suggestions that the Auditor-Controller provided during their visit, as well as other suggestions from housing finance specialists working with accounting firms. Recent comments received from outside specialists suggest that our cost-benefit approach is reasonable and meets or exceeds industry standards.

The Asset Management Policies and Procedures, Section II.E, specifies the informational fields that, at a minimum, must be documented by each reviewer, most of which are generated automatically by the Asset Management Database (AMD) when notes are entered. Hard copies of the tracking notes are printed, as required.

45. **RECOMMENDATION:** Ensure developers submit separate residual receipt calculations.

RESPONSE: HDP will utilize the Residual Receipt Calculation Detail (RRCD) form as an attached schedule to the audited or reviewed Financial Statement, which will allow the appropriate information to be evaluated and tied into the AFS.

46. **RECOMMENDATION:** Ensure staff with sufficient accounting or financial knowledge review the residual receipt calculations and follow up timely on discrepancies between reported and expected results.

RESPONSE: In order to fulfill this recommendation, the Housing Development and Preservation Division will coordinate with the Financial Management Division staff and, where appropriate, utilize outside consultants to review recommendations made by the Housing Development and Preservation staff. This is the current process outlined in the revised Asset Management Policies and Procedures, which have been developed mindful of the cost efficiencies discussed above. The Residual Receipt Calculation Detail form has been developed to solicit Borrower information in an appropriate format that helps to clarify the review process. Additionally, all involved staff has recently undergone training and these efforts will continue.

47. **RECOMMENDATION:** Consider reviewing all Industry loans to determine if developers correctly reported and paid residual receipts to date, and require developers to pay CDC the required portion of residual receipts, if any.

RESPONSE: As part of HDP's annual developer notification, a letter requesting audited financial statements and completion of the RRCD form will be sent to all developers in order the HDP may receive information for the purpose of determining any residual receipts payable for the 2003 and 2004 calendar years. Given the relative newness of completed Industry-funded developments, we feel that this is a sufficient look-back period to determine a pattern of operating and other associated costs. Based upon our review, we may choose to request information for previous years as is appropriate. Where indicated and consistent with HDP's cost-benefit approach, the Commission will take action to collect residual receipts.

48. **RECOMMENDATION:** Develop and implement written procedures for monitoring Industry loans for residual receipts.

RESPONSE: The Commission is currently implementing written procedures for monitoring all of its loan programs as part of its Strategic Planning Process.

COUNTY BUSINESS LOAN PROGRAM

Business Administration Plan

49. **RECOMMENDATION:** CDC management update the CBLP Plan to reflect CDC's current business practices and obtain EDA Approval.

RESPONSE: The County Business Loan Program (CBLP) was established for the purpose of *assisting aerospace/defense firms that were negatively impacted by the decline in federal defense spending*. The definition of the program should be revised in the Auditor Controller's report to accurately reflect its purpose. In addition, it should be noted that *the CBLP can make loans to businesses in the entire Los Angeles Urban County*, not just in the unincorporated areas as stated in the report.

The stated purpose of the audit is to "determine if CDC awards loans in a fair, accurate and appropriate manner to minimize the risk of loss". Based on the success of the program, it can be concluded that the CBLP has exceeded its established goals, as supported by the following results:

Life-to-date, CBLP financing has permitted companies to create or retain over 750 jobs.

Life-to-date, CBLP revenue, from interest and fee income, exceeds \$2,048,000.

Life-to-date, CBLP revenue has exceeded all expenses, direct and overhead, by \$893,523.

Moreover, the CBLP has awarded loans in a fair, accurate and appropriate manner, while *minimizing the risk of loss*. The Auditor Controller notes that the "CDC's default rate of 2% for the CBLP compares favorably with other government funded loans programs which have default rates ranging from 23% to 44%."

While unidentified in the report, the government funded loan program with the 23% loss rate is the nationwide CDBG lending program, and the government funded loan program with the 44% default rate is the Los Angeles Community Development Bank.

The Auditor-Controller's report requests that the Commission update the CBLP Administrative Plan (the Plan). The Commission previously provided information to the Auditor Controller demonstrating numerous attempts to update the Plan, which have been denied by the U.S. Department of Commerce, Economic Development Administration (EDA). The EDA funds the Commission's four revolving loan funds and must approve revisions to the Plan. EDA also requires reauthorization, though federal statute, every five years. Following the audit, EDA was reauthorized by Congress, which would permit revolving loan fund operators to merge multiple revolving loan funds into a single fund. The Commission was previously informed by EDA that it would not consider amendments to any Administrative Plan until the passage of the reauthorization bill.

The Commission submitted Administrative Plans for amendment in 1999, 2000 and 2003, but did not receive approval from EDA. At the request of the Auditor Controller, a revised Administrative Plan was submitted in August 2004, and review was again declined by EDA. Now with the reauthorization approval, the Commission will submit an Administrative Plan for amendment.

Compliance with Business Administration Plan

- 50. RECOMMENDATION:** CDC management ensure loan files and data supplied to the Loan committee is complete and in compliance with the Plan. Departures from current policy should be documented and justified in the applicant's loan file.

RESPONSE: The report states: "One of the three applicants did not submit a business plan with financial projections indicating the business' future fiscal viability." Two of the applicants submitted business plans and the third, which had been in business for 10 years prior to its application, submitted a history of the firm and principals. That submittal meets requirements, as the practice of commercial/industrial lending does not typically require a formal business plan for an on-going operation.

The report also states: "Two (67%) of the three credit memorandums did not contain a statement indicating that the applicant was unable to obtain private financing." For one company, a statement indicating the applicant was unable to obtain private financing was in the loan file, and this information was provided orally to the Loan Committee.

Finally, the report states: "...one (50%) of the two instances, there was no documentation in the loan file substantiating the applicant's inability to obtain

private financing.” This information was conveyed to the Loan Committee during consideration of the loan. Data supplied to the Loan Committee are complete. We acknowledge the need for notes to the loan file for clarification purposes.

Monitoring Process

- 51. RECOMMENDATION:** Ensure loan files contain sufficient documentation to indicate that loan requirements (i.e., job created condition) have been met.

RESPONSE: The report states: “Two (67%) of three loan files did not contain proof that the jobs created condition....was met.” One of the firms in question did not provide the proof of job creation, and this information was transmitted to the Auditor-Controller during the week of September 13, 2004, which was during the period of the audit review. In addition, the debt obligation of the firm in question and the associated job creation requirement was retired by conversion to equity interest through the granting of warrants to the Commission. In other words, the Commission took an equity position (ownership) in the firm, prior to the audit. Copies of the conversion documents were provided the Auditor-Controller. The second firm received a working capital loan in 1994. Job creation for this loan was to occur during the seven-year term of the loan. The firm filed a Chapter 7 Bankruptcy in 1997, and at that time the firm had not met job creation requirements. Such bankruptcy extinguished both the monetary and regulatory requirements of the debt. Therefore, no job creation documentation was possible.

The Commission is already in compliance with Recommendation 51.

- 52. RECOMMENDATION:** Ensure staff conduct and document financial analyses to determine a business’ ability to meet it future financial obligations under the loan.

RESPONSE: The report states: “One (33%) of the three loan files did not submit all financial statements as required.” Clarification is requested from the Auditor Controller regarding the name of the company in question. However, if the Auditor-Controller is referring to the 1994 loan that went bankrupt and was charged off in 1997, there would be no subsequent financials in the file.

The report also states: “For all three (100%) of the loans reviewed, CDC staff did not document financial statement analyses in the loan files.” This statement is not accurate. Financial analysis was performed and incorporated into each loan file.

The Commission already conducts the necessary analyses and reviews. Documentation may be required in some instances.

- 53. RECOMMENDATION:** Require staff to annually obtain and review proof of each business' hazard and liability insurance.

RESPONSE: The report states: "In two (67%) of the three loans reviewed, CDC staff did not have current proof of hazard and liability insurance." Currently, the Commission sends a letter semi-annually to borrowers requesting proof of hazard and liability insurance. Copies of the standard letter of request were provided to the Auditor-Controller.

In the future, the Commission will more diligently enforce obtaining proof of business hazard and liability insurance from borrowers. This will be delineated in the new agency-wide Loan Approval and Collection Policy that is currently undergoing executive level review.

- 54. RECOMMENDATION:** Initiate action on delinquent loans in a timely manner.

RESPONSE: The report states: "In one (33%) of three loans reviewed, CDC did not initiate legal action for approximately three years from the date the business became delinquent." The Auditor-Controller was fully informed about the exceptional nature of the loan in question, from our point of view. This loan was deemed by others to have the potential for considerable public benefit through job creation and training of disadvantaged youth. Because of the social purpose of this loan in particular, the Commission had to be a patient lender.

The Auditor-Controller was also informed that the Commission had secured an executed forbearance agreement with a new repayment schedule from the firm. Further, the Auditor-Controller was informed that the Commission had structured the loan so that the CBLP had the guarantees of all the principals and their spouses, which increases the probability of collection in the case of default. This information should be taken into account when evaluating why the Commission was willing to work with the firm as it attempted to restructure and reposition itself, and why the Commission reluctantly was forced to seek legal action.

The Commission will continue to evaluate delinquent loans on a case-by-case basis, including carefully weighing the particular circumstances of each borrower and other mitigating factors. As part of the responsible management of loans funds, we feel that it is appropriate to consider the social, economic and other benefits that these loans represent within the communities served.

END